EXTRACT FROM BY-LAWS

Section 9. No book shall, at any time, be taken from the Library Room to any other place than to some court room of a Court of Record, State or Federal, in the City of San Francisco, or to the Chambers of a Judge of such Court of Record, and then only upon the accountable receipt of some person entitled to the use of the Library. Every such book so taken from the Library, shall be returned on the same day, and in default of such return the party taking the same shall be suspended from all use and privileges of the Library until the return of the book or full compensation is made therefor to the satisfaction of the Trustees.

Sec. 11. No books shall have the leaves folded down, or be marked, dog-eared, or otherwise soiled, defaced or injured. Any party violating this provision, shall be liable to pay a sum not exceeding the value of the book, or to replace the volume by a new one, at the discretion of the Trustees or Executive Committee, and shall be liable to be suspended from all use of the Library till any order of the Trustees or Executive Committee in the premises shall be fully complied with to the satisfaction of such Trustees or Executive Committee.

No. 10393

United States

Circuit Court of Appeals

For the Ninth Circuit.

KENNETH BENJAMIN EDWARDS,

Appellant,

vs.

UNITED STATES OF AMERICA,

Appellee.

Transcript of Record

Upon Appeal from the District Court of the United States for the Southern District of California, Central Division

Rotary Colorprint, 590 Folsom St., San Francisco

No. 10393

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[Clerk's Note: When deemed likely to be of an important nature, errors or doubtful matters appearing in the original certified record are printed literally in italic; and, likewise, cancelled matter appearing in the original certified record is printed and cancelled herein accordingly. When possible, an omission from the text is indicated by printing in italic the two words between which the omission seems to occur.]

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NAMES AND ADDRESSES OF ATTORNEYS:

For Appellant:

A. L. WIRIN

257 S. Spring St.
Los Angeles, Calif.

For Appellee:

CHARLES H. CARR,

United States Attorney

BETTY MARSHALL GRAYDON,

Assistant United States Attorney
600 U. S. Post Office and Court House Bldg.
Los Angeles, Calif. [1*]

*Page numbering appearing at foot of page of original certified Transcript of Record.

United States District Court, Southern District of California, Central Division.

No. 15800

THE UNITED STATES OF AMERICA

vs.

KENNETH BENJAMIN EDWARDS

INDICTMENT

(Viol.: 50 U.S.C. App. 311)

No. 15800 Filed 1-20-43

Viol.: United States Code, Appendix, Title 50, Section 311.

In the District Court of the United States in and for the Southern District of California, Central Division, September, 1942 Term

In the Name and by the Authority of the United States of America, the Grand Jury for the Southern District of California, at Los Angeles, presents on oath in open court:

That

KENNETH BENJAMIN EDWARDS,

hereinafter called the defendant, is a male person within the class made subject to selective service under the Selective Service Act of 1940, as amended;

that defendant registered as required by the Selective Training and Service Act of 1940 and the rules and regulations promulgated thereunder and became a registrant of Local Board No. 170, said board being then and there duly created and acting under the Selective Service System established by said Act in the County of Orange, State of California, in the division and district aforesaid; that pursuant to the terms and provisions of said Act, and the rules and regulations promulgated thereunder, the said defendant was classified by said local board in Class 4-E and was subsequently notified of said classification by said board and a notice and order by said board was thereafter duly given to said defendant to report for work of national importance in lieu of induction into the armed forces of the United States of America on June 1, 1942, at Orange, California, within the district and division aforesaid; that said defendant did at said time and place knowingly, wilfully, unlawfully and feloniously fail and neglect to perform a duty required of him under said Act and the rules and regulations promulgated thereunder, that is to say the defendant did then and there knowingly, wilfully, unlawfully and feloniously fail to report for work of national importance in lieu of induction into the armed forces of the United States as so notified and ordered to do;

Contrary to the form of the statute in such case made and provided and against the peace and dignity of the United States of America.

LEO V. SILVERSTEIN
United States Attorney [2]

A true bill,

ROY D. BAYLY
Foreman.

Bail, $1000.

[Endorsed]: Filed Jan. 20, 1943. [3]

At a stated term, to wit: The February Term, A. D. 1943 of the District Court of the United States of America, within and for the Central Division of the Southern District of California, held at the Court Room thereof, in the City of Los Angeles on Monday the 1st day of February in the year of our Lord one thousand nine hundred and forty-three.

Present:

The Honorable: Leon R. Yankwich, District Judge.

No. 15,800—Crim.

[Title of Cause.]

PLEA OF NOT GUILTY

This cause coming on for arraignment and plea of the defendant Kenneth Benjamin Edwards; H. P. Bledsoe, Esq., Assistant U. S. Attorney, appear-

ing for the Government; Samuel Goldstein, Court Reporter, being present and reporting the proceedings; A. L. Wirin, Esq., appearing as counsel for the defendant; the defendant being present in Court on bond, now states his true name to be as charged in the Indictment, waives the reading of the Indictment, and pleads not guilty to the charges contained in the Indictment; it is ordered that this cause be, and it hereby is, set for trial on March 2, 1943.

MB 31/794 [4]

[Title of District Court and Cause.]

VERDICT

We the jury in the above entitled cause find the defendant Kenneth Benjamin Edwards guilty as charged in the indictment.

Los Angeles, California, March 3, 1943.

S. ALLEN GREER
Foreman of the Jury.

[Endorsed]: Filed Mar 3 1943. [5]

District Court of the United States, Southern District of California, Central Division

UNITED STATES

v.

KENNETH BENJAMIN EDWARDS

No. 15800. Criminal indictment in 1 counts for violation of U.S.C., Title 50, Secs. 311.

JUDGMENT AND COMMITMENT

On this 15th day of March 1943, came the United States Attorney, and the defendant Kenneth Benjamin Edwards appearing in proper person, and with counsel and,

The defendant having been convicted on verdict of the jury of the offense charged in the indictment in the above-entitled cause, to wit on June 1 1942 at Orange, California, defendant failed to report for work of national importance in lieu of induction into the armed forces of the United States as so notified and ordered to do.

and the defendant having been now asked whether he has anything to say why judgment should not be pronounced against him, and no sufficient cause to the contrary being shown or appearing to the Court, It Is by the Court

Ordered and Adjudged that the defendant, having been found guilty of said offenses, is hereby committed to the custody of the Attorney General for imprisonment in an institution of the jail type to

be designated by the Attorney General or his authorized representative for the period of one year.

It Is Further Ordered that the Clerk deliver a certified copy of this judgment and commitment to the United States Marshal or other qualified officer and that the same shall serve as the commitment herein.

(Signed) LEON R. YANKWICH
United States District Judge.

[Endorsed]: Filed this 15th day of March 1943.

[6]

[Title of District Court and Cause.]

NOTICE OF APPEAL

Name and address of Appellant: Kenneth Benjamin Edwards, Route 1, Box 477 B, Orange, California.

Name and address of Appellant's attorneys: A. L. Wirin, 257 South Spring Street, Los Angeles, California.

Offense: Violation of Selective Training and Service Act of 1940.

Date of Judgment: March 15, 1943.

Brief discription of judgment or sentence: Imprisonment of one year in a prison of a penitentiary type.

Name of prison where now confined: Los Angeles County Jail.

I, the above-named Appellant, hereby appeal to the United States Circuit Court of Appeals for the

Ninth Circuit from the judgment above mentioned on the grounds set forth below.

Dated: March 16, 1943.

KENNETH B. EDWARDS
Appellant. [7]

GROUNDS OF APPEAL:

1. The Court erred in refusing to grant defendant's requested instructions as excepted to.

2. The Court erred in giving instructions submitted by the prosecution as excepted to by defendant.

3. The Court erred in ruling upon evidence and rejection of proffered exhibits by defendant and rejecting defendant's offers of proof, as excepted to by defendant.

4. The evidence was insufficient to justify a conviction.

5. The judgment abridges the petitioner's liberty without due process of law.

A. L. WIRIN
Attorney for Appellant.

[Endorsed]: Filed Mar 16, 1943. [8]

[Title of District Court and Cause.]

ORDER ALLOWING RELEASE ON BAIL, ON APPEAL

The defendant having filed a notice of appeal to the Ninth Circuit Court of Appeals, and good cause

appearing therefor, it is hereby ordered that the defendant may be released upon bail, on appeal, in the sum of $1000.

Dated: At Los Angeles, this 16th day of March, 1943.

LEON R. YANKWICH
United States District Judge.

[Endorsed]: Filed Mar. 16, 1943. [9]

[Title of District Court and Cause.]

BAIL BOND ON APPEAL

Know All Men by These Presents:

That we, Kenneth Benjamin Edwards, of the County of Los Angeles, as principal and Floyd E. Edwards, Louise Edwards, and Evelyn M. Trueblood, all of Orange County, California, as sureties, are held and firmly bound unto the United States of America, in the sum of One Thousand Dollars, to the payment of which, well and truly to be made, we jointly and severly bind ourselves, our heirs, executors, administrators and assigns, firmly by these presents.

Witness our hands and seals at Los Angeles, in said District, this 16th day of March, 1943.

The conditions of the above obligation *is* such that,

Whereas, lately, to wit, on the 15th day of March, 1943, at a term of the District Court of the United States, in and for the Southern District of Cali-

fornia, Central Division, in an action pending in the said court in which the United States of America [10] was plaintiff and Kenneth Benjamin Edwards was defendant, a judgment and sentence was made, given, rendered and entered against the said Kenneth Benjamin Edwards, in the above entitled action, wherein he was convicted as charged of violation of the Selective Training and Service Act of 1940;

Whereas, in said judgment and sentence so made, given, rendered and entered against the said Kenneth Benjamin Edwards, he was by said judgment sentenced to imprisonment for a period of one year in an institution of a penitentiary type;

Whereas, the said Kenneth Benjamin Edwards has been admitted to bail pending the decision upon said appeal, in the sum of One Thousand ($1,000.00) Dollars.

Now, Therefore, the conditions of this obligation are such that if said Kenneth Benjamin Edwards shall appear in person, or by his attorney, in the United States Circuit Court of Appeals for the Ninth Circuit on such day or days as may be appointed for the hearing of said cause in said Court and prosecute his appeal; and if the said Kenneth Benjamin Edwards shall abide by and obey all court orders made by the said United States Circuit Court of Appeals for the Ninth Circuit, and if the said Kenneth Benjamin Edwards shall surrender himself in execution of said judgment and sentence, if the said judgment and sentence be affirmed by the said United States Circuit Court of Appeals

for the Ninth Circuit; and if the said Kenneth Benjamin Edwards will appear for trial in the District Court of the United States, in and for the Southern District of California, Central Division, on such day or days as may be appointed for retrial by said District Court, and if the said judgment and sentence against him be reversed, then this obligation shall be null and void; otherwise to remain in full force and effect.

This Recognizance shall be deemed and construed to contain the "express agreement", summary judgment and execution thereon, mentioned in Rule 13 of the District Court. [11]

KENNETH BENJAMIN EDWARDS
Principal
R. D. #1, Box 478-A
Orange, Calif.
Address

LOYD E. EDWARDS
R. D. 1, Box 477B
Orange, California
Address

LOUISE EDWARDS
R. D. 1, Box 477B,
Orange, Calif.
Address

EVELYN M. TRUEBLOOD
R. D. #1, Box 478-A,
Orange, Calif.
Address

Approved as to form

LEO V. SILVERSTEIN
U. S. Attorney
By: HOWARD T. CALVERLEY,
Asst. U. S. Attorney

I hereby certify that I have examined the within bond and that in my opinion the form hereof is correct, and sureties thereon are qualified.

A. L. WIRIN
Attorney for Defendant and Appellant.

ORDER

The foregoing bond is approved this 16th day of March, 1943.

LEON R. YANKWICH
United States District Judge.

[12]

United States of America,
Southern District of California

Loyd E. Edwards, Louise Edwards of Orange County, Calif. and Evelyn M. Trueblood of Orange County, Calif. each being duly sworn, deposes and says:

That each is a householder in the District aforesaid, and is worth the sum of One Thousand Dollars, over and above all debts and liabilities, exclusive of property exempt from execution, and is the owner of the property listed below under Schedule of Assets, which schedule is made a part of this affidavit; that the said property is not encumbered

except as below listed and that the property is reasonably of the value below listed, and further that he is not receiving or accepting compensation for acting as surety herein and is not surety upon any outstanding penal bonds except as disclosed in the schedule below.

(A) LOYD E. EDWARDS (Seal)
LOUISE EDWARDS (Seal)
(B) EVELYN M. TRUEBLOOD (Seal)

Subscribed and sworn to before me this 16th day of March 1943.

B. B. HANSEN
United States Commissioner for the Southern District of California

SCHEDULE OF ASSETS

Sureties "A"

Tract No. 918 N2 AC Lot 34 5 AC in 35 and 5 AC in 38, Orange County, California N.W. ¼, Sec. 25 TWP 4 R9, no encumbrances, valued at $20,000.

Surety "B"

4.68 AC In N.W. ¼ Sec. 25 TWP 4 R9, Tract 918, Orange County, California. No encumbrance—valued at $5,000.

[Endorsed]: Filed Mar. 16, 1943. [13]

[Title of District Court and Cause.]

STIPULATION re EXHIBITS

It is hereby stipulated that the original Exhibits introduced into evidence or marked for identification may be transmitted to the Appellate Court.

Dated this 12 day of July, 1943.

CHARLES H. CARR
United States Attorney
By BETTY MARSHAL GRAYDON
Assistant United States Attorney
A. L. WIRIN
Atty. for defendant

It is so ordered.

LEON R. YANKWICH
Judge

Received copy of the within stipulation, July 12, 1943.

BETTY MARSHAL GRAYDON
Assistant U. S. Atty.

[Endorsed]: Filed Jul 12 1943. [14]

[Title of District Court and Cause.]

STIPULATION AND ORDER

It Is Stipulated that the appellant may have to and including June 15, 1943, within which to have settled and filed bill of exceptions herein.

Dated this 7 day of April, 1943.

A. L. WIRIN
Attorney for Appellant
LEO V. SILVERSTEIN
United States Attorney
By BETTY MARSHALL GRAYDON
Assistant United States Attorney,
Attorneys for Appellee

ORDER

Good cause appearing therefor, and based upon the foregoing stipulation, [15]

It Is Ordered that the appellant may have to and including June 15, 1943, within which to have settled and filed bill of exceptions herein.

Dated this 7 day of April, 1943.

LEON R. YANKWICH
Judge.

[Endorsed]: Filed April 7, 1943. [16]

[Title of District Court and Cause.]

THE STATEMENT OF POINTS AND DESIGNATION OF PARTS OF THE RECORD AND STIPULATION

Appellant states that he intends to rely on all the points set out in his assignment of errors.

The appellant hereby designates the following documents to be included in the printed transcript of the record:

1. Indictment
2. Arraignment and Plea
3. Verdict
4. Judgment and Sentence
5. Notice of Appeal
6. Order extending time to settle and file Bill of Exceptions
7. Bill of Exceptions
8. Assignment of Errors
9. Stipulation that Exhibits may be transmitted to the Appellate Court.

A. L. WIRIN
Attorney for Defendant [17]

[Title of District Court and Cause.]

STIPULATION

It is hereby stipulated that the foregoing Statement of Points and Designation of Parts of the Record include all documents to be included in the printed transcript of the record.

Dated this 12 day of July, 1943.

CHARLES H. CARR
United States Attorney
By BETTY MARSHALL GRAYDON
Assistant United States Attorney

Received copy of the within Statement and Stipulation July 12, 1943.

BETTY MARSHAL
GRAYDON
Asst. U. S. Attorney

[Endorsed]: Filed July 12, 1943. [18]

[Title of District Court and Cause.]

CERTIFICATE OF CLERK

I, Edmund L. Smith, Clerk of the District Court of the United States for the Southern District of California, do hereby certify that the foregoing pages numbered from 1 to 18 inclusive contain full, true and correct copies of: Indictment; Minute Order entered February 1, 1943; Verdict; Judgment and Commitment; Notice of Appeal; Order Allowing Release on Bail on Appeal; Bail Bond on Appeal; Stipulation and Order for Transmission of Original Exhibits; Stipulation and Order Extending Time to Settle and File Bill of Exceptions and Statement of Points and Designation of Parts of the Record and Stipulation which, together with the Original Bill of Exceptions, Original Assignment of Errors and Original Exhibits transmitted herewith constitute the record on appeal to the Circuit Court of Appeals for the Ninth Circuit.

I further certify that my fees for comparing, correcting and certifying the foregoing record amount to $4.60 which sum has been paid to me by Appellant.

Witness my hand and the seal of said District Court this 24 day of July, 1943.

[Seal] EDMUND L. SMITH, Clerk
By THEODORE HOCKE
Deputy Clerk.

At a Stated Term, to wit: The October Term 1943 of the United States Circuit Court of Appeals for the Ninth Circuit, held in the Court Room thereof, in the City and County of San Francisco, in the State of California, on Monday the fourteenth day of June in the year of our Lord one thousand nine hundred and forty-three.

Present:

Honorable Curtis D. Wilbur, Senior Circuit Judge, Presiding,
Honorable Francis A. Garrecht, Circuit Judge,
Honorable William Healy, Circuit Judge.

No. 10393

KENNETH BENJAMIN EDWARDS,
Appellant,

vs.

UNITED STATES OF AMERICA,
Appellee.

ORDER EXTENDING TIME TO SETTLE AND FILE BILL OF EXCEPTIONS

Upon consideration of the stipulation of counsel for respective parties, and affidavit of Mr. A. L.

Wirin in support thereof, filed June 14, 1943, and good cause therefor appearing, it is Ordered that the time within which appellant may settle and file his bill of exceptions in this cause be, and hereby is extended to and including July 15, 1943.

I hereby certify that the foregoing is a full, true, and correct copy of an original Order made and entered in the within-entitled cause.

Attest my hand and the seal of the United States Circuit Court of Appeals for the Ninth Circuit, at the City of San Francisco, in the State of California, this 14th day of June, 1943.

(Seal) PAUL P. O'BRIEN,

Clerk, U. S. Circuit Court of Appeals for the Ninth Circuit.

[Endorsed]: Filed Jun 15 1943.

In the United States District Court, Southern District of California, Central Division

No. 15800 Criminal

UNITED STATES OF AMERICA,

Plaintiff,

vs.

KENNETH BENJAMIN EDWARDS,

Defendant.

BILL OF EXCEPTIONS

Be it remembered that the above entitled case came on for trial on March 2, 1943, before the

Hon. Leon R. Yankwich presiding in Courtroom No. 5, of the District Court of the United States, for the Southern District of California, Central Division, sitting with a jury.

The United States of America, Plaintiff, appeared by Leo V. Silverstein, United States Attorney, and Betty Marshall Graydon, Assistant United States Attorney, and the Defendant was represented by A. L. Wirin. The following proceedings were had and the following evidence both oral testimony and by stipulation was received, to-wit:

IDA K. LEHR,

called for the Government, testified that the defendant was classified "1B" on October 17, 1941, and appealed the classification. The Appeal Board reclassified defendant "4E" on February 16, 1942. That defendant was directed to appear at the Local Board #170 on June 1, 1942, at 4:30 P. M. to be examined and to be instructed as to his duties. That he had been assigned to the Civilian Public Service Camp. Defendant appeared on that day and refused to go to camp. That he was thereafter notified again to report to the Board but did not do so and has never reported to camp. The defendant in his questionnaire and in his letters claimed he should be classified "4D" on the grounds he was an ordained minister of Jehovah's Witnesses. In his questionnaire he admitted working on his father's farm for his living and spending as much time as possible performing services

(Testimony of Ida K. Lehr.)

in various capacities as a member of Jehovah's Witnesses. Affidavits had been filed with the Board stating that the defendant was an ordained minister of Jehovah's Witnesses. Defendant filed with his questionnaire the special form for Conscientious Objectors, Form 47.

The Local Board had information, through a letter dated October 22, 1941, that defendant was not listed in the official certified list of Jehovah's Witnesses.

Outside the presence of the jury, the Court stated that he would not permit the question to go to the jury as to whether the Local Board acted arbitrarily.

Defendant offered in evidence a document dated June 25, 1942, which was refused admission into evidence by the Court upon objection by the Government that it is dated after defendant's classification. This document was subsequently marked defendant's Exhibit I for identification. [2*]

In the examination of

CHARLES W. GRIFFITH,

the following occurred: He testified that he was a special agent of the Federal Bureau of Investigation and that defendant signed a statement in writing voluntarily.** In this statement defendant admitted that he had refused to report to any camp on the ground that he was an ordained min-

*Page numbering appearing at foot of page of original Bill of Exceptions.

**This document was introduced as Exhibit 9.

ister. Upon the conclusion of the testimony of Charles W. Griffith, the Government rested.

Defendant called

KENNETH B. EDWARDS,

the defendant, as a witness. He testified that in the past year he averaged 150 hours a month preaching the Gospel as a minister of Jehovah's Witnesses. That he has also served in the capacity as back-call servant. That he is at present a "pioneer" and devotes his full time to preaching the Gospel. That he has been a "pioneer" for almost a year having become a "pioneer" in March of the preceding year. That he became a member and minister of Jehovah's Witnesses in 1938. That from 1938 to 1939 he worked on his father's farm part time. That in 1940 he was working 32 hours a week on the farm and was preaching 10 hours a week; that in 1941 he was preaching about 15 hours a week and was working on the farm about 28 hours a week; that in 1942 he devoted 36 hours to preaching per week and during the last part of 1942 he was devoting all of his time to preaching. That he had always planned on devoting full time to Jehovah's Witnesses and went into the pioneer work when he felt he owed no more obligation to his father. That on March 25, 1942, he sent a letter to the Local Board, a copy of which was introduced in evidence as defendant's Exhibit "D". This is a letter of defendant in which he states that he was appointed a "pioneer" by the

(Testimony of Kenneth B. Edwards.)

Watch Tower Bible and Tract Society, Inc. on March 5, 1942, and that he was devoting his full time as a minister of Jehovah's Witnesses and that his name would soon be added to the certified list of Pioneers on [3] file with the National and State Headquarters of the Selective Service System. It further states that he was entitled to a "4D" classification. The witness stated that he did not receive a reply from the Board to that letter. A letter of defendant dated May 25, 1942, defendant's Exhibit "F", was admitted into evidence. In this letter, defendant stated that as he informed the Board in his letter of March 25, 1942, he was a full time ordained minister of Jehovah's Witnesses and that he asked the Board to defer final action on his case until National Headquarters Selective Service had an opportunity to rule on his case. Exhibit "E" was received in evidence and is a document directed to State Headquarters of Selective Service and a copy of which was enclosed with Exhibit "F", and defendant therein states he was appointed a full time "pioneer" by the Watch Tower Bible and Tract Society, Inc. on March 5, 1943, and that he has been devoting, as such "pioneer", 150 hours in said Service per month besides service in other capacities. That he devotes his full time to the Lord's work. He requested an appeal to avoid an injustice. A letter from the Local Board dated May 29, 1942, was received in evidence as Exhibit "G". This letter states that the Board never re-

(Testimony of Kenneth B. Edwards.)
ceived defendant's letter of March 25, 1942, and that defendant took his case out of the hands of the Board when he appealed to the Board of Appeals. Defendant admitted that he appeared at the office of the Local Board on June 1, 1942, and refused to go to camp on the grounds that his work as a minister of Jehovah's Witnesses would not permit him to do so; he testified that he did not intend to commit a felony when he refused to go to camp but intended to obey God's law; that he did not believe the order was lawful or valid.

On cross-examination defendant stated that he did not rely upon earthly ordination to make him an ordained minister and that he did not follow a course of study in a theological school. That he was not a full time minister when he filed his questionnaire; [4] the following testimony was then given:

Q. By Mrs. Graydon: Did you read the order of induction for Work of National Importance when you received it? A. Yes.

Q. And you also read the Notice of Suspected Delinquency? A. Yes, I did.

Q. And you read the statement that failure to report on or about the day and hour prescribed is an offense punishable by fine or imprisonment, or both? A. Yes, and I so reported.

Q. Did you also know that it was an offense not to obey an induction order, as stated on your

(Testimony of Kenneth B. Edwards.)

order, for work, that wilful failure to report directly to your own local Board at the hour and on the day named in the notice is a violation of the Selective Training and Service Act of 1940 and subjects you to a fine and imprisonment?

A. Yes, and so I reported as designated there, at the time.

Q. But you did not report for Work of National Importance?

The Court: (Interposing) You reported to them that you were not going? A. Yes.

Q. By Mrs. Graydon: Well, now that you have come to court and found through the experience you passed through, since you did not report for induction, you do know now that it is a violation of the law, do you not?

A. Yes, a violation of the order which I do not believe was properly enacted.

Q. By Mrs. Graydon: Are you still of the same frame of mind? A. Yes, I am.

On re-direct examination, defendant stated that he never asked [5] for a classification of "4E", but always asked the classification of "4D".

On re-cross-examination, Mrs. Graydon asked the following question "Do you think that you did not have a fair hearing?" The Court refused to permit the question on its own initiative in the following language "I'm not going to permit that question to be answered. I am not going to have the jury pass on the question of whether it is a

(Testimony of Kenneth B. Edwards.)
fair hearing. That is not their province. The only thing they have to determine is whether there was a violation and if it was willful."

MRS. LOUISE EDWARDS

was examined as a witness on behalf of the defendant. She testified that she was the mother of the defendant. That she has been a member of Jehovah's Witnesses for a long time. That defendant became a "pioneer" in March, 1942.

DWIGHT T. KENYON

was called as a witness by defendant. He stated that he was a member of Jehovah's Witnesses. That defendant has been a member of Jehovah's Witnesses since 1934, and has held his religious views since that time.

VICTOR OCHSNER

was called as a witness by defendant. He stated that he had a conversation with M. B. Wellington, chairman of the Local Draft Board, in which Mr. Wellington spoke of Jehovah's Witnesses and stated that "I think the organization is rotten. It stinks. The whole organization stinks. It is a

(Testimony of Victor Ochsner.)

disgrace to Christianity. I have no use for it at all." Upon objection by Mrs. Graydon, the Court struck the question and answer as immaterial and not impeachment and further that the conversation had nothing to do with this particular classification. The following testimony was then given:

The Court: By the way, the conversation had nothing to do with any discussion about this Edwards case, or any other case?

The Witness: No, it was a general conversation. [6]

Mrs. Graydon: I object to it, your Honor.

The Court: Well, you didn't object to it at the beginning. I will strike the question and answer as immaterial, it is not impeachment, Mr. Wellington hasn't testified as a witness and furthermore this is a conversation which had nothing to do with this particular classification.

Mr. Wirin: May I ask a question that does have to do with it?

The Court: We are not trying the mental attitude of this man because the man wasn't before the Court as a witness. If he had been before the Court and testified you could ask questions that would impeach him.

Mr. Wirin: We take an exception to the Court, on its own motion, striking the answer.

The Court: The motion has been made. I didn't rule on it, you followed it up so fast I didn't have time to rule on it. I have a right to ask to strike questions and answers on my own motion. After all, I can object myself if the United States

(Testimony of Victor Ochsner.)
Attorney doesn't protect me. I don't allow such questions and if the United States Attorney doesn't protect and is asleep at the switch I can object.

Mr. Wirin requested the Court if he could ask a question that had to do with this particular classification. The Court answered "We are not trying the mental attitude of this man because the man wasn't before the Court as a witness. If he had been before the Court and testified you could ask questions that would impeach him." Mr. Wirin thereupon took exception to the Court, striking the answer. The Court thereupon instructed the jury to disregard the question and answer. Mr. Wirin then stated "What, if anything, was said during the course of the conversation concerning persons who [7] were members of Jehovah's Witnesses having claimed exemption before the Draft Board of which Mr. Wellington was a member?" Mrs. Graydon objected that it was incompetent, irrelevent, and immaterial. The Court sustained the objection. Mr. Wirin asked if he could make an offer of proof that the conversation pertained to the ministers of Jehovah's Witnesses, but Court then stated that he would sustain an objection to the offer of proof and told the jury to disregard it.

Mr. Wirin then stated he would call Richard Ochsner. The Court then stated "If you are going to ask the same questions, I won't allow the same questions to be asked. I have ruled on it and I will not allow those questions to be gone into."

RICHARD J. OCHSNER

was called as a witness for defendant. Mr. Wirin made an offer of proof that this witness would testify substantially as did Victor Ochsner. The Court then stated it would sustain the objection to the offer of proof and ordered the jury to disregard it on the ground it was not material with the issue involved in this case.

FLOYD BUMPHRY

was called as a witness by defendant. Mr. Wirin made an offer of proof to prove by this witness and also by C. W. Council, who was in Court, that there was a conversation of October 16, 1942, in the course of which Mr. Rodieck, a member of the Draft Board involved in this proceeding, expressed himself as hostile and antagonistic to Jehovah's Witnesses. The Court sustained the objection to an offer of proof on the ground that it was immaterial to the issue and could not impeach any particular member of the Board because such member was not a witness in this case. Mr. Wirin further stated that the prejudice, which these witnesses expressed, afterwards had roots in the minds of the other members of the Board.

After the jury was excused, Mr. Wirin made a motion for a directed verdict. The motion was denied and exception was granted to defendant. [8]

The Court then instructed the jury.

Mr. Wirin excepted to the court's refusal to give the requested instructions Numbers 7 to 30 inclusive. Mr. Wirin also excepted to instructions requested by the prosecution and given by the Court, 3, 4, 5, 6, and 7. The exceptions were noted by the Court.

The following is Instruction Number 7 as requested by the defendant:

"You are instructed that although under the Act, the decision as to what classification a particular registrant is to receive is left to the local board, this does not mean that a court of law does not have the power nor that you as a jury do not have the power to review a classification.

This review is limited, however, to a determination by the jury of the facts, subject to the limitations to be indicated by the Court in later instructions, that constitute arbitrariness or capriciousness, denial by the draft board of a fair hearing, or violation by the draft board of the provisions of the Selective Training and Service Act, or the Rules and Regulations adopted pursuant to that Act."

The following are instructions 8 to 30 inclusive as requested by defendant and which were not given by the Court:

8. Arbitrary power and the rule of the United States Constitution requiring the principle of fair play (legally known as "due process") cannot both exist at the same time. They are antagonist and incompatible forces. Of necessity arbitrary power must perish before the rule of the Constitution.

There is no place in our constitutional system of government (and this includes the administration of the Selective Service System) for the exercise of arbitrary power.

9. You are instructed that Local and Appeal Boards under [9] the Selective Service System must not act in an arbitrary or capricious manner. Classifications by such boards must be based upon the evidence before them and that evidence alone.

If you find that the local and appeal boards in this case acted in an arbitrary or capricious manner or disregarded the evidence that was before them or failed to give the registrant, defendant here, a full and fair hearing, you will acquit the defendant and find him not guilty.

10. You are further instructed more particularly that if the order of the local or appeals boards in classifying the defendant was made arbitrarily or capriciously, or was the result of passion or prejudice; or was made in disregard of the evidence presented to it, or if there was not substantial evidence to sustain the finding of the local board; or if the defendant was denied any hearing at all; or was denied a full and fair hearing, the order of the local or appeal board in ordering the defendant to report for induction into the armed forces was an illegal order since it was made as a result of the deprivation of the defendant of his rights of due process of law.

It is for the jury to determine the facts as whether any of the above took place in the case of the defendant.

11. If you find that the local board acted arbitrarily or capriciously in classifying the defendant as it did, you will find the defendant not guilty.

12. If you find that the decision of the local or appeal board was arrived at because of passion or prejudice [10] against the Defendant or against Jehovah's Witnesses, you will find the Defendant not guilty.

13. If you find that there was not substantial evidence before the boards to sustain the finding that Defendant should be classified as he was, you will find the Defendant not guilty.

By substantial evidence is meant a large quantum of evidence. It does not mean an absence of evidence and it means more than just a scintilla or some evidence. It means that there must be enough evidence before the boards so that a reasonable man in the same circumstances as presented in this case would come to the same conclusion as the boards did. If there was not enough of such evidence before the local or appeal board, you must acquit the Defendant.

14. If you find that the local or appeal board disregarded the evidence presented on behalf of the Defendant, you will find the Defendant not guilty.

15. The denial of a full and fair hearing is the same thing as the denial of any hearing. Therefore, if you find that although the Defendant was granted a hearing, if that hearing was not a full and fair one but was merely perfunctory and was not in accord with the ordinary rules of decency

and fair play, or not in accord with the Selective Service System Rules and Regulations, you will find the Defendant not guilty.

16. If you find that the Defendant was not granted any hearing before the local board although he requested one, you must find the Defendant not guilty.

17. Under the Selective Training and Service Act and its Rules and Regulations, a registrant is given a right of appeal from a classification of a local draft board, [11] to an appeals board.

This right may not be arbitrarily or capriciously taken away from a registrant.

18. The Selective Training and Service Act of 1940 and the regulations promulgated pursuant thereto provide that ministers of religion are exempt from training and service under the Act.

19. Under the Act there are two kinds of ministers of religions regular ministers of religion and duly ordained ministers of religion.

A regular minister of religion is a man who customarily preaches and teaches the principles of religion of a recognized church, religious sect, or religious organization of which he is a member, without having been formally ordained as a minister of religion; and who is recognized by such church, sect, or organization as a minister.

A duly ordained minister of religion is a man who has been ordained in accordance with the ceremonial ritual or discipline of a recognized church, religious sect, or religious organization, to teach and preach its doctrines and to administer its rites

and ceremonies in public worship; and who customarily performs these duties.

20. The rule that ministers of religion are exempt from training and service under the act means that if a person is a minister of religion, an order by his local board to report for induction into the armed forces of the United States is of no force or effect. This is so because a local board has no jurisdiction to order a minister of religion to report for service in the armed forces. [12]

21. The Jehovah's Witnesses constitute a recognized religious organization within the meaning of the Selective Training and Service Act.

22. If you find that the Defendant at the time of his classification customarily preached and taught the principles of the beliefs of Jehovah's Witnesses and that the Defendant was a member of Jehovah's Witnesses and that the organization of the Jehovah's Witnesses recognized the Defendant as a minister and that from the facts presented to the local board reasonable men could not have found otherwise, you will find the Defendant Not Guilty.

23. The Court and the Jury may take judicial notice of the Selective Training and Service Act and of the Rules and Regulations thereunder, issued by the President of the United States and the Director of the Selective Training and Service System; that the Director thereof, Lewis B. Hershey, issued the following regulation pertaining to the ministerial status of Jehovah's Witnesses.

The regulation is as follows: (the regulation is attached hereto and marked Exhibit "A")

The regulation has the full effect of law and was and is binding upon the local draft boards and appeals boards of the Selective Training and Service System.

24. You are instructed that Paragraph 626.1(a) of the Regulations promulgated pursuant to the Selective Training and Service Act of 1940, reads as follows:

"Classification not permanent. (a) No classification is permanent."

25. You are instructed that Paragraph 626.2(a) of the Regulations promulgated pursuant to the Selective [13] Training and Service Act of 1940, reads as follows:

"(a) The local board may reopen and consider anew the classification of a registrant (1) upon the written request of the registrant, the government appeal agent, any person who claims to be a dependent of the registrant, or any interested party in a case involving occupational deferment, if such request is accompanied by written information presenting facts not considered when the registrant was classified which, if true, would justify a change in the registrant's classification: or (2) upon its own motion if such action is based upon facts not considered when the registrant was classified which, if true, would justify a change in the registrant's classification; provided, in either event, the classification of a registrant shall not be reopened after the local board has mailed to such

registrant an Order to Report for Induction (Form 150) unless the local board first specifically finds there has been a change in the registrant's status resulting from circumstances over which the registrant had no control."

26. You are instructed that Paragraph 626.3 of the Regulations promulgated pursuant to the Selective Training and Service Act of 1940, reads as follows:

"Refusal to reopen and consider anew registrant's classification. When a registrant, any person who claims to be a dependent of a registrant, any interested party in a case involving occupational deferment, or the government appeal agent files with the local board a written request to reopen and consider anew the registrant's classification and the local board is of the opinion that the information accompanying such re- [14] quest fails to present any facts in addition to those considered when the registrant was classified, or, even if new facts are presented, the local board if of the opinion that such facts, if true, would not justify a change in such registrant's classification. In such a case, the local board, by letter, should advise the person filing the request that the information submitted does not warrant the reopening of the registrant's classification and should place a copy of the letter in the registrant's file. No other record of the receipt of such a request and the action taken thereon is required."

27. You are instructed that Paragraph 626.11 of the Regulations promulgated pursuant to the

Selective Training And Service Act of 1940, reads as follows:

"When Classification reopened, it shall be considered anew. When the local board reopens the registrant's classification, it shall consider the new information which it has received and shall again classify the registrant in the same manner as if he had never before been classified, provided that if he has been physically examined, the examining physician's Report of Physical Examination and Induction (Form 221), already in his file, shall be used to determine whether he has any defect set forth in Part I or Part II of the List of Defects (Form 220) when such fact is necessary in order to complete his classification. Such classification shall be and have the effect of a new and original classification even though the registrant is again placed in the class that he was in before his classification was reopened."

28. You are instructed that Paragraph 626.12 of the Regulations [15] promulgated pursuant to the Selective Training and Service Act of 1940, reads as follows:

"Notice of action when classification considered anew. When the local board reopens the registrant's classification, it, as soon as practicable after it again classifies the registrant, shall mail notice thereof on the Notice of Classification (Form 57) to the registrant and on Classification Advice (Form 59) to the person entitled to receive such notice or advice on an original classification under the provisions of section 623.61."

29. You are instructed that Paragraph 626.13 of the Regulations promulgated pursuant to the Selective Training and Service Act of 1940, reads as follows:

"Right of appeal following reopening of classification. Each such classification shall be followed by the same right of appearance before the local board and the same right of appeal as in the case of an original classification."

30. You are instructed that Paragraph 642.3 of the Regulations promulgated pursuant to the Selective Training and Service Act of 1940, reads as follows:

"Disposition of delinquencies. If a suspected delinquent has been located as a result of the local board's efforts under section 242.2 or a suspected delinquent has reported voluntarily to a local board, the local board shall carefully investigate the delinquency. If the board finds that the suspected delinquent is innocent of any wrongful intent, the local board shall proceed to consider his case just as if he were never suspected of being a delinquent. The local board shall report its decision to the State Director of Selective [16] Service and shall note its decision in its records."

The following are instructions 3 to 7 inclusive, given by the Court as requested by the prosecution, and duly excepted to by the Defendant:

3. It is beyond your province to inquire into the policy of the law. It is also beyond your province to determine whether the law should have excluded persons other than those it does exclude

from its provisions. The only question you are called to determine is whether the law has been violated knowingly and willfully.

4. The President is authorized to select and induct into the armed forces of the United States for training and service those registrants who have been selected in an impartial manner under such rules and regulations as the President may prescribe.

At all times mentioned in the indictment the Selective Training and Service Act of 1940, among other things, required the registration of every male person residing in the United States between the ages of 21 and 35, inclusive, and likewise provided that a limited class of human beings should be subject to Selective Service, namely, with few exceptions, the class of male humans residing within the United States between the ages of 20 and 44, inclusive.

The Act further authorizes the President to prescribe the necessary rules and regulations to carry out the Act, and to establish Selective Service civilian boards, including Local Boards and Appeal Boards. The Local Boards under the terms of the Act, have power to hear and determine all questions or claims with respect to induction in or exemption or deferment from training and service, and the decision of such local boards are final except [17] where an appeal is authorized in accordance with such rules and regulations as the President may prescribe. Various classifications for exceptions, exemptions, and defer-

ments are set up in the Act. It is provided that any person who is, by reason of religious training and belief, conscientiously opposed to participation in war of any form, shall not be required to be subject to combatant training and service, and if classified as such a "conscientious objector" he shall be assigned to noncombatant service.

It is further provided in the Act that if any person is conscientiously opposed to participation in war in any form and is also conscientiously opposed to participation in noncombatant service, and if he is so classified by a local board, then he shall be assigned to work of national importance under civilian direction, in lieu of induction into the armed forces for either combatant or noncombatant service.

If any registrant is dissatisfied with his classification by his local board, or if his claim for exemption from combatant or noncombatant service is denied by such local board, then he may appeal to his appropriate appeal board.

5. You are not sitting as a court of appeal to determine whether the local board or the appeal board was right in its determination of the classification of the defendant. The actions of the local board and the appeal board were gone into merely for the purpose of showing what opportunity was afforded to the defendant to present his proof for the classification he claimed. So that from it and all the remainder of the evidence in the case, you may determine whether there was a refusal or neglect on the part of the defendant to do what

the law required of him [18] and whether if you find beyond a reasonable doubt that there was such refusal or neglect, the defendant did so refuse or neglect knowingly and wilfully as these words have been defined by us.

6. In other words, what you are required to determine beyond a reasonable doubt, and it is your exclusive province to determine, is whether or not the defendant after registering and being classified IV-E, Conscientious Objector, by his local board and after being assigned to report for work of national importance, did knowingly fail to respond to the board's order to report for work of national importance. In determining this you may consider any matters in the record other than those mentioned which might indicate to you the lack of intent on the part of the defendant to disregard the board's order.

7. This is an offense requiring a specific intent. When this is the case, the intent must be shown to exist beyond a reasonable doubt. The intent may be shown by the acts and declarations of the defendant and by the circumstances surrounding his actions. They must, when taken together, prove the specific intent which, in this case, is to knowingly fail or neglect to submit to induction when notified to do so.

As bearing upon the question of the intent of the defendant he has testified to his reasons for his actions. You are to consider them in that connection only. However, if you are convinced beyond a reasonable doubt that the defendant did

in fact fail to submit to induction and that in so doing, he acted wilfully and with the knowledge that he was refusing to obey an act which he was required by law to perform, then his belief that his actions, if any, may have been justified by his religious beliefs is immaterial. [19] Religious belief does not excuse a violation of the law, if it be shown beyond a reasonable doubt that such violation of law actually occurred, and was wilful.

And it is for you to determine, in the light of all the evidence in the case, whether such wilful violation has occurred.

The foregoing Bill of Exceptions was prepared within the time allowed by law, as extended, and correctly sets forth the proceedings and evidence in connection with said trial and therefore settled, allowed and approved.

Dated this 13th day of July, 1943.

LEON R. YANKWICH

Judge of the District Court

[20]

[Title of District Court and Cause.]

STIPULATION

It is hereby stipulated that the foregoing Bill of Exceptions is correct and may be allowed. That a copy of the same was received.

Dated: July 12 1943.

CHARLES H. CARR
United States Attorney
By BETTY MARSHALL GRAYDON
Assistant United States Attorney

Acknowledgment of service of copy of within Bill of Exceptions. Dated: July 12, 1943.

BETTY MARSHALL GRAYDON
Asst. U. S. Attorney

[Endorsed]: Filed July 13, 1943.

[Title of District Court and Cause.]

ASSIGNMENT OF ERRORS

Appellant in the above entitled action assigns as error the following:

(2) The refusal to permit any inquiry into whether defendant had a fair hearing.

(3) The striking out of the question and answer asked Victor Ochsner in regard to the statements made by M. B. Wellington, chairman of the Local Draft Board.

(4) The refusal to permit questions to be asked Richard Ochsner in regard to statements made by M. B. Wellington about his attitude towards Jehovah's Witnesses after an offer of proof by A. L. Wirin.

(5) The sustaining of an objection of an offer of proof that Floyd Bumphry would testify that Mr. Rodieck, a member of the Draft Board, expressed himself as hostile and antagonistic towards Jehovah's Witnesses.

(6) The giving of instructions by the Court that the decisions of the Local Board are final.

(7) Giving of instructions by the Court that the jury could not determine whether the Local Board or the Appeal Board was right in its determination of the classification of defendant.

(8) The giving of instructions 3, 4, 5, 6, and 7 requested by the prosecution.

(9) The refusal to give instructions 7 to 30 inclusive requested by the defendant.

(10) The judgment of conviction violates the rights of the defendant to freedom of religion.

Dated this 12 day of July, 1943.

A. L. WIRIN

Attorney for Defendant.

Received copy of the within Assignment of Errors: July 12, 1943.

BETTY MARSHALL
GRAYDON
Asst. U. S. Attorney

[Endorsed]: Filed July 13, 1943.

[Endorsed]: No. 10393. United States Circuit Court of Appeals for the Ninth Circuit. Kenneth Benjamin Edwards, Appellant, vs. United States of America, Appellee. Transcript of Record. Upon Appeal from the District Court of the United States for the Southern District of California, Central Division.

Filed July 26, 1943.

PAUL P. O'BRIEN
Clerk of the United States Circuit Court of Appeals for the Ninth Circuit.

United States Circuit Court of Appeals
for the Ninth Circuit

No. 10393

KENNETH BENJAMIN EDWARDS,
Appellant,

vs.

UNITED STATES OF AMERICA,
Appellee.

STATEMENT OF POINTS UPON WHICH PETITIONER INTENDS TO RELY ON APPEAL

Petitioner hereby adopts as his point on appeal the assignments of error included in the petition for review within the transcript of record.

A. L. WIRIN
Attorney for Appellant.

[Title of Circuit Court of Appeals and Cause.]

DESCRIPTION OF PARTS OF RECORD TO BE PRINTED

The petitioner hereby designates for printing the entire transcript of record.

Dated at Los Angeles, California, July 29, 1943.

A. L. WIRIN
Attorney for Appellant

(Affidavit of Service by Mail to Betty Marshall Graydon, Asst. U. S. Atty. by copy being placed in mail Aug. 2, 1943 by A. L. Wirin.)

[Endorsed]: Filed Aug. 10, 1943. Paul P. O'Brien, Clerk.

[Title of Circuit Court of Appeals and Cause.]

STIPULATION RE NON PRINTING OF EXHIBITS

It is stipulated that the exhibits in the above entitled case on appeal may be filed with the clerk of this Court, and need not be printed.

A. L. WIRIN
Attorney for Appellant

CHARLES H. CARR
United States Attorney
BETTY MARSHALL GRAYDON
By BETTY MARSHALL GRAYDON
Assistant United States Attorney

So Ordered:

FRANCIS A. GARRECHT
United States Circuit Judge

[Endorsed: Filed Sept. 7, 1943. Paul P. O'Brien, Clerk.

No. 10393.

IN THE

United States Circuit Court of Appeals

FOR THE NINTH CIRCUIT

KENNETH BENJAMIN EDWARDS,

Appellant,

vs.

UNITED STATES OF AMERICA,

Appellee.

APPELLANT'S OPENING BRIEF.

A. L. WIRIN,
257 South Spring Street, Los Angeles,
Attorney for Appellant.

Parker & Baird Company, Law Printers, Los Angeles

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No. 10393.

IN THE

United States Circuit Court of Appeals

FOR THE NINTH CIRCUIT

KENNETH BENJAMIN EDWARDS,

Appellant,

vs.

UNITED STATES OF AMERICA,

Appellee.

APPELLANT'S OPENING BRIEF.

Jurisdictional Statement.

This is an appeal from a judgment of convictions of the appellant by the District Court for the Southern District of Califora, and a jury thereof. This court has jurisdiction under the provisions of 28 United States Code, Section 225, subdivision (a), First and Third and subdivision (d).

Statement of the Case.

The appellant, one of the Jehovah's Witnesses, was convicted in the court below for a violation of the Selective Training and Service Act under an indictment [R. 2] which charged him with having "knowingly, wilfully, unlawfully and feloniously" failed to comply with an order of his local draft board.

In the court below, and before the Selective Service Agencies, he claimed to be both a duly ordained and regular minister, and hence entitled to a classifiaction as such under the Selective Training and Service Law.

Before his local board he asserted that he was a "full timed ordained minister of Jehovah's Witnesses" [R. 23], and he submitted evidence to his board that he was a full time "Pioneer," devoting 150 hours a month to his work as a minister, besides serving in other capacities; that he devoted full time to the Lord's work. [R. 23.]

At the trial the appellant claimed that he had not received a fair hearing before his local board or the Selective Agencies. The trial court refused to permit evidence to this effect, and on its own motion stated in the presence of the jury, "I'm not going to permit that question to be answered. I am not going to have the jury pass on the question of whether it is a fair hearing. That is not their province. The only thing they have to determine is whether there was a violation and if it was wilful." [R. 25.]

The trial court refused evidence proffered by the appellant that the members of the appellant's local draft board were prejudiced against Jehovah's Witnesses. [R. 26-29.]

Requested instructions proffered by the appellant, were rejected by the trial court. To this rejection the appellant duly excepted. The instructions so refused are:

> "You are instructed that although under the Act, the decision as to what classification a particular registrant is to receive is left to the local board. this does not mean that a court of law does not have the power nor that you as a jury do not have the power to review a classification.

"This review is limited, however, to a determination by the jury of the facts, subject to the limitations to be indicated by the Court in later instructions, that constitute arbitrariness or capriciousness, denial by the draft board of a fair hearing, or violation by the draft board of the provisions of the Selective Training and Service Act, or the Rules and Regulations adopted pursuant to that Act."

"You are instructed that local and appeal boards under the Selective Service System must not act in an arbitrary or capricious manner. Classifications by such boards must be based upon the evidence befor them and that evidence alone.

"If you find that the local and appeal boards in this case acted in an arbitrary or capricious manner or disregarded the evidence that was before them or failed to give the registrant, defendant here, a full and fair hearing, you will acquit the defendant and find him not guilty.

"You are further instructed more particularly that if the order of the local or appeal boards in classifying the defendant was made arbitrarily or capriously, or was the result of passion or prejudice; or was made in disregard of the evidence presented to it, or if there was not substantial evidence to sustain the finding of the local board; or if the defendant was denied any hearing at all; or was denied a full and fair hearing, the order of the local or appeal board in ordering the defendant to report for induction into the armed forces was an illegal order since it was made as a result of the deprivation of the defendant of his rights of due process of law."

"It is for the jury to determine the facts as whether any of the above took place in the case of the defendant."

Similar instructions, along the same lines were also rejected by the trial court [R. 32-33].

Amongst other instructions given by the Court, and duly excepted to by the appellant were: "The only question you are called to determine is whether the law has been violated knowingly and wilfully." [R. 39.]

Question Involved.

May a defedant charged with a violation of the Selective Training and Service Act assert as a defense to a criminal prosecution for failure to comply with an order of a local draft board, that the order which he is charged with having violated was unlawful because it was arbitrary or capricious, without evidentiary support, or without a hearing.

Specification of Assigned Errors to Be Relied Upon.

1. The refusal of the trial court to permit any inquiry as to whether appellant had a fair hearing before the Selective Service Agencies. [R. 43.]

2. The refusal of the trial court to allow any inquiry as to whether the members of the appellant's local draft board were prejudiced against Jehovah's Witnesses.

3. The refusal of the trial court to give instructions requested by the appellant, to the effect that the appellant could assert as a defense that he had been denied a fair hearing by the Selective Service Agencies and that they had acted arbitrarily and capriciously and without any or substantial evidence in refusing to classify the appellant as a minister within the Selectrive Training and Service Act. [R. 43.]

ARGUMENT.

I.

Determinations of Local Selective Service Boards Are Subject to Judicial Review, if Such Decisions Abridge Due Process, Are Made Upon the Denial of a Fair Hearing, Are Unsupported by Evidence or Arbitrary or Capricious, or Violate Law.[1]

That order of local draft boards are subject to judicial review is a proposition supported by many cases;[2] and generally no longer challenged.

This rule of law puts life and reality into the well recognized judicial concept, so well expressed in *Jones v. Securities and Exchange Commission,* 298 U. S. 1, 23:

> ". . . Arbitrary power and the rule of the Constitution cannot both exist. They are antagonistic and incompatible forces; and one or the other must of necessity perish wherever they are brought into conflict. To borrow the words of Chief Justice Day—'There is no place in our constitutional system for the exercise of arbitrary power.'"

It is equally well put by Chief Justice Hughes in *Morgan v. United States,* 304 U. S. 1, who recognized that the

> "vast expansion of administrative agencies makes necessary that in administrative proceedings of a

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[1]The answer to this precise question is being awaited from the United States Supreme Court in *Falbo v. United States,* October Term 1943, No. 73.

[2]They are cited and considered in detail in *Okrand, Judicial Review of Selective Service Board Classifications,* Southern California Law Review, November, 1942.

Cf. also Yankwich, J., in *Ex parte Stewart,* 47 F. Supp. 410.

quasi-judicial character the liberty and property of the citizen shall be protected by the rudimentary requirements of fair play."

At another point the Court observed:

"If these multiplying (administrative) agencies deemed to be necessary in our complex society are to serve the purposes for which they are created and endowed with vast powers, they must accredit themselves by acting in accordance with the cherished judicial tradition embodying the basic concepts of fair play."

St. Joseph Stockyards v. United States, 298 U. S. 38, is in similar accord.

II.

The Selective Service System Is an Administrative and Quasi-Judicial System, and Therefore Is Governed by the Law Governing Judicial Review of Administrative or Quasi-Judicial Bodies.

In *Angelus v. Sullivan,* 246 Fed. 54, 63 (C. C. A. 2, 1917), speaking of the 1917 Draft Act, the Court said:

"The law courts have a general superintending control by certiorari over all inferior tribunals acting in a judicial or quasi-judicial character. Civil jurisdiction is not entirely taken away by the words of a statute which declares that the judgment of the inferior tribunal shall be final."

Again in *Arbitman v. Woodside,* 258 Fed. 441, 442 (C. C. A. 4, 1919), we find:

"The rule is established that the action of such executive boards (draft boards) within the scope of their authority is final, and not subject to judicial

review, when the investigation has been fair and the finding supported by substantial evidence; but upon proof that the investigation has not been fair, or that the board has abused its discretion by a finding contrary to all the substantial evidence, relief should be given by the courts under the writ of *habeas corpus.*"

III.

It Is the Accepted Administrative Law Rule That, as a Defense to a Criminal Prosecution for Violation of an Order of an Administrative Board, the Validity of the Board's Order May Be Challenged, Particularly Where the Board Has Offended the Rudimentary Demands of Justice Incorporated in the Concept "Due Process."

(1) The United States Supreme Court Cases.

The particular question involved in this appeal has not been directly passed upon by the Supreme Court. That Court, however, has on at least four occasions intimated its views on the problem, two of the cases being criminal prosecutions for violations of administrative orders.

Thus, *Union Bridge Co. v. United States,* 204 U. S. 364, was a criminal prosecution against a bridge company for its failure to obey the order of the Secretary of War to remove an obstruction to navigation by making higher a bridge. This order of the Secretary of War was made pursuant to the power vested in him by Section 18 of the Act of March 3, 1899 (30 Stat. at L. 1121, 1153). The Secretary gave notice, conducted hearings, considered the evidence, and then made his order. Upon the company's failure to comply, the United States Attorney in the district was notified and a criminal prosecution was insti-

tuted. (Note the similarity in procedure to that under the Selective Training and Service Act.) In deciding that the Act did not improperly delegate authority to the Secretary of War, the Court pointed out that the Act did not give the Secretary arbitrary power but only the power to act reasonably. Said the Court significantly:

> ". . . Nor is there any reason to say that the Secretary of War was not entirely justified, if not compelled, by the evidence in finding that the bridge in question was an unreasonable obstruction to commerce and navigation as now conducted." (p. 307.)

Again in *Monongahela Bridge Co. v. United States,* 216 U. S. 177 (1910), the same objections were raised as in the *Union Bridge Company* case. The Court decided similarly, observing:

> "It does not appear that the Secretary disregarded the facts, or that he acted in an arbitrary manner, or that he pursued any method not contemplated by Congress."

And, accordingly upheld the conviction.

Thus the Court observed that arbitrariness on the part of the Secretary of War was a proper matter of defense.

Looking into the future, when counsel suggested extreme cases of arbitrariness, the Court commented, at page 195:

> "It will be time enough to deal with such cases as and when they arise. Suffice it to say that the courts have rarely, if ever, felt themselves so restrained by technical rules that they could not find some remedy, consistent with the law, for acts, whether done by government or by individual per-

sons, that violated natural justice or were hostile to the fundamental principles devised for the protection of the essential rights of property."

It can thus be seen from the above, although *dicta,* that the Supreme Court was of the opinion that if it were shown that the action of the administrative officer were arbitrary, such evidence would be considered by the Court *in a criminal prosecution,** in determining whether the defendant's constitutional rights had been abridged.

In two other cases involving enforcement of administrative determinations, although not criminal prosecutions, the Supreme Court has indicated that administrative arbitrariness is a defense to enforcement proceedings.

In *Hagar v. Reclamation District No. 108,* 111 U. S. 701 (1834), the Court said:

". . . The assessment under consideration could, by the law of California, be enforced only by legal proceedings, and *in them any defense going either to its validity or amount could be pleaded.*"

Again in *Bradley v. City of Richmond,* 227 U. S. 477 (1913), another administrative enforcement action, the Court commented:

". . . Obviously the burden was upon the plaintiff in error to show an illegal and capricious classification."

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*All italics ours.

(2) State Courts Have Directly Ruled That Such a Defense Is Available.

The highest courts of several states have ruled that proper administrative law principles direct the availability of the defense.

(a) New York.

Fire Department of New York v. Gilmour, 149 N. Y. 453, 44 N. E. 177, was an action to enforce a penalty for violation of an order of the fire department of the City of New York, requiring removal of dangerous and combustible material. The trial court excluded evidence as to the propriety and reasonableness of the order on the ground that such matter was not a proper defense to the action. In reversing the trial court, the New York Court of Appeals said:

> ". . . The justice refused to hear the evidence, saying, 'The question before the court is, has there been a refusal to comply with the order of the board? The court regrets that it can't go into the question whether the order was necessary or whether the department acted properly.'
>
> "We think the justice erred in the principle upon which he proceeded.
>
> ". . . where the legislature . . . invests a subordinate body with the power to investigate and determine the fact whether in any special case any use is made of property for purposes of storage, dangerous on account of its liability to originate or extend a conflagration . . . then we are of the opinion that in such cases the reasonableness of the determination of the board or of the order prohibiting a particular use in accordance with such determination, is open to contestation by the party affected

thereby, and that he is entitled, when sued for disobedience of the order, to show that it was unreasonable, unnecessary and oppressive."

McLean v. Jephson, 123 N. Y. 142, 25 N. E. 409; and *Board of Health v. Heister,* 37 N. Y. 661 (1868), are in accord.

(b) Massachusetts.

The highest court of the State of Massachusetts, in *Stevens v. Casey,* 228 Mass. 368, 117 N. E. 528, spoke on the problem in the following language:

". . . Doubtless if the landowner had not sought a review by the Superior Court of the action of the inspector in accordance with the terms of the statute, he would have a right to a trial by jury as to the existence of the fundamental facts upon which the jurisdiction of the inspector rested, *when a criminal prosecution* or proceeding in equity were instituted against him for failure to comply with the requirements imposed by the inspector."

(c) Illinois.

In *People v. McCoy,* 125 Ill. 289, 17 N. E. 786 (1888), the defendant was an M. D. and continued to practice medicine after the state board of health had taken his license away. This action was a criminal prosecution for practicing medicine without a license. In ruling that the administrative order was invalid because it was not supported by the evidence, the Court declared:

"The board cannot from mere caprice, or without cause, revoke a certificate fairly issued upon sufficient evidence of the applicant's qualifications."

(3) The English Rule Is in Accord.

In *Waye v. Thompson,* L. R. 15 Q. B. 342 (1885), the law in question provided that the inspector of meats had the power to determine that meat was unfit. If he made such a determination, he brought the meat before a magistrate who heard the inspector. If the magistrate was satisfied that the meat was unfit for human consumption. he ordered it destroyed and the owner of the meat was thereupon subject to imprisonment. This is a proceeding on an order to show cause as to why the defendant should not be put in jail. The lower court permitted evidence as to the condition of the meat at the time it was condemned; was satisfied that the meat was not unwholesome and gave judgment to the defendant with costs. On appeal the plaintiff-appellant argued that the Court of Petty Sessions (the trial court) was not a court of appeal to review the decision that the meat was bad; in the criminal proceeding the owner could show that the meat had not been exposed for sale or that it was not intended as food for man, but the decision that the meat was unfit for human use was final and conclusive. The Court of Queen's Bench overruled the plaintiff's argument and upheld the decision of the lower court in permitting the evidence in.

(4) Text Writers Are in Accord.

In his exhaustive article, *"Statutory Roads to Review of Federal Administrative Orders,"* appearing in 28 California Law Review 129, 163, Mr. Beck P. McAllister says:

> ". . . If no form of statutory *judicial* review is available there is every reason to say that review should be had in the criminal court. . . ."

See also article by United States District Judge R. C. Bell, American Bar Association Journal, March, 1942, page 164.

Conclusion.

Involved in this appeal, is the recurring issue of religious liberty asserted by one of Jehovah's Witnesses. It must be remembered that the Supreme Court in recent years has extended and restored to its "high constitutional position, the liberties of itinerant evangelists"[1] of which the appellant is one; that freedom of religion is in a "preferred position."[2]

We are dealing here with one of the freedoms which is "the matrix, the indispensable condition of nearly every other form of freedom."[3]

Respectfully submitted,

A. L. WIRIN,
Attorney for Appellant.

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[1]Justice Douglas speaking for the Court in *Murdock v. Pennsylvania*, 87 L. Ed. (Adv. Op.) 827, at 834.

[2]Justice Douglas, *supra*, at page 833.

[3]Justice Cardozo, in *Palko v. Connecticut*, 302 U. S. 219.

No. 10393.

IN THE

United States Circuit Court of Appeals

FOR THE NINTH CIRCUIT

KENNETH BENJAMIN EDWARDS,

Appellant,

vs.

UNITED STATES OF AMERICA,

Appellee.

APPELLEE'S BRIEF.

CHARLES H. CARR,
United States Attorney;

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Appellee.

APPELLEE'S BRIEF.

Jurisdiction.

This case was tried in the United States District Court in and for the Southern District of California, upon whom jurisdiction was conferred by Section 41(2) of Title 28 of the United States Code. This Court has appellate jurisdiction under the provisions of Section 225(a) of Title 28 of the United States Code to review the judgment of the District Court.

Statement of Case.

Appellant has substantially stated the case in his Opening Brief, to which appellee will add the following:

Not until March 5, 1943, after defendant had been classified 4-E (conscientious objector) on February 16,

1942, by the Appeal Board, and after he had been ordered entrained on June 1, 1942, did he attempt to submit proof to his local board that he was a full time "Pioneer." [R. 23.] Appellant's statement on page 2 (second paragraph) of his brief does not make the time element clear.

In the ensuing paragraph, appellant states that at the trial appellant claimed that he had not received a fair hearing before his local board or the Selective Agencies. Nowhere in his direct testimony [R. 22-26] did the defendant himself so testify or so claim, although in the recross-examination of the defendant by the Government attorney, the Court did not permit the defendant to answer the question: "Do you think that you did not have a fair hearing?"

Question Involved.

Appellant has stated the question involved as follows:

> May a defendant charged with a violation of the Selective Training and Service Act assert as a defense to a criminal prosecution for failure to comply with an order of a local draft board, that the order which he is charged with having violated was unlawful because it was arbitrary or capricious, without evidentiary support, *or without a hearing?* (Emphasis supplied.)

The record does not disclose that the appellant was denied a hearing.

Appellant's argument is presented under three heads, as follows:

> I. Determinations of Local Selective Service Boards Are Subject to Judicial Review, if Such De-

cisions Abridge Due Process, Are Made Upon the Denial of a Fair Hearing, Are Unsupported by Evidence or Arbitrary or Capricious, or Violate Law.

II. The Selective Service System Is an Administrative and Quasi-Judicial System, and Therefore Is Governed by the Law Governing Judicial Review of Administrative or Quasi-Judicial Bodies.

III. It Is the Accepted Administrative Law Rule That, as a Defense to a Criminal Prosecution for Violation of an Order of an Administrative Board, the Validity of the Board's Order May Be Challenged, Particularly Where the Board Has Offended the Rudimentary Demands of Justice Incorporated in the Concept "Due Process."

We believe appellant's argument is conclusively answered by the recent decision of the Supreme Court of the United States in the case of *Nick Falbo, Petitioner, v. The United States of America,* No. 73, October Term 1943, decided January 3, 1944. This case is determinative of similar issues as are involved in the case before this Court.

We rely on the law in the *Falbo* case, as expressed by Justice Black, as follows:

> Even if there were, as the petitioner argues, a constitutional requirement that judicial review must be available to test the validity of the decision of the local board, it is certain that Congress was not required to provide for judicial intervention before final acceptance of an individual for national service. The narrow question therefore presented by this case is whether Congress has authorized judicial review of the propriety of a board's classification in a criminal

prosecution for wilful violation of an order directing a registrant to report for the last step in the selective process.

We think it has not. The Act nowhere explicitly provides for such review and we have found nothing in its legislative history which indicates an intention to afford it. The circumstances under which the Act was adopted lend no support to a view which would allow litigious interruption of the process of selection which Congress created. To meet the need which it felt for mobilizing national manpower in the shortest practicable period, Congress established a machinery which it deemed efficient for inducting great numbers of men into the armed forces. Careful provision was made for fair administration of the Act's policies within the framework of the selective service process. But Congress apparently regarded "a prompt and unhesitating obedience to orders" issued in that process "indispensable to the complete attainment of the object" of national defense. Martin v. Mott, 25 U. S. 19, 30. Surely if Congress had intended to authorize interference with that process by intermediate challenges of orders to report, it would have said so.

Against this background the complete absence of any provision for such challenges in the very section providing for prosecution of violations in the civil courts permits no other inference than that Congress did not intend they could be made.

This would appear to answer completely all the questions and arguments raised by appellant.

Conclusion.

Now that the Supreme Court has spoken, it is respectfully urged that the appellant has no recourse to the courts and no right of judicial review unless and until he has complied with all orders of the local draft board, in this instance, to have reported himself for transportation to a conscientious objector's camp in compliance with the order of the draft board.

Respectfully submitted,

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IN THE

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KENNETH BENJAMIN EDWARDS,

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APPELLANT'S REPLY BRIEF.

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APPELLANT'S REPLY BRIEF.

The appellant exhausted all administrative steps within the Selective Service system[1] *and accordingly was in a position to challenge the arbitrariness of the action of the Selective Service agencies in failng to clasisfy him as a regular or duly ordained minister.*

The appellant did not, as did *Nick Falbo*, fail to comply with the order of his board. On the contrary, he complied with it—in that he appeared at the time and place directed in the draft boards order, which he is charged with having violated.

In so reporting, pursuant to the terms of his draft board's order, the appellant took the final step within the Selective Service system to be entitled to challenge the classification in the courts by interposing as a defense

[1]As outlined and required by the Supreme Court in *Falbo v. United States*, 320 U. S. 549, and *Billings v. Truesdell*, 88 L. Ed. (Adv. Op.) 573 (decided March 27, 1944).

to the indictment the arbitrariness and unfairness of his classification. In the *Falbo* case the Supreme Court said:

> "The narrow question therefore presented by this case is whether Congress has authorized judicial review of the propriety of a board's classification in a criminal prosecution for wilfull violation of an order directing a registrant to report for the *last step* in the Selective Service process." (Italics ours.)

In the case at bar, appellant took that "last step" so as to be in a position to challenge the propriety of his classification by the Selective Servce agencies. Again in the *Billings* case the court (at page 581 of 88 L. ed.) reasserted the views expressed by it in the *Falbo* case as to what steps a registrant must take within the Selective Service system to be entitled to defend against an indictment charging a violation of an order by local draft board, where the registrants claim is that the order was void. Said the Court:

> "Moreover, it should be remembered that he who reports at the induction station is following the procedure outlined in the *Falbo Case* for the exhaustion of his administrative remedies. Unless he follows that procedure he may not challenge the legality of his classification in the courts."

The clear import of the *Falbo* and *Billings* decisions is that one who *has* followed the procedure within the Selective Service system by taking and thus exhausting all the administrative steps, then places himself in a position to defend, in the event of a criminal prosecution for a volation of an order of the Selective Service agencies, on the ground that the order offended due process, was arbitrary, or otherwise void.

Otherwise, as the court put it in the *Billings* case (at page 581 of 88 L. ed.) the *Falbo* case becomes a "trap."

> "That would indeed make a trap of the Falbo Case by subjecting those who reported for completion of the Selective Service process to more severe penalties than those who stayed away in defiance of the board's order to report."

The appellant appeared at the office of his local board on June 1, 1942, as directed in the order [R. 24]. As testified by him: "Yes and so I reported as designated there (in the order) at the time." [Rep. 25.] This was admitted by government witness Ida K. Lehr (local draft board clerk), "Defendant appeared on that date and refused to go to camp." [R. 20.]

Although the appellant, by thus reporting, brought himself squarely within the *Falbo* case, the trial court by its rulings upon evidence and its instructions and failure to give instructions expressly ruled that the appellant was not in a position to assert the abritrariness of the action of the Selective Service agencies as a defense. With respect to the question of a fair hearing before the Selective Service agencies the trial court advised the jury:

> "I am not going to have the jury pass on the question of whether it is a fair hearing. That is not their province. The only thing they have to determine is whether there was a violation and if it was wilfull." [R. 25, 26.]

Consistent with this position the trial court ordered stricken, testimony to the effect that the chairman of the appellant's local draft board stated of Jehovah's Witnesses,

> "I think the organization is rotten, it stinks. The whole organization stinks. It is a disgrace to Christianity. I have no use for it at all." [R. 26, 27.]

The trial court additionally refused the proffer of similar testimony from other witnesses. [R. 28, 29.] In the refusal of instructions proffered by the appellant, particularly instructions No. 7, 9, 10, 11, 12, 13, 14 and 15[2] [R. 30-33], the trial court removed from the case, and prevented the jury from passing upon, the appellant's substantive defense.

Conclusion.

Thus the appellant, by the trial court's rulings was, in effect, deprived of his "day in court," by being denied the right to interpose a substantial defense. The judgment of conviction and sentence accordingly deprive him of liberty without due process of law, and should be reversed.[3]

Respectfully submitted,

A. L. Wirin,
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Hayden C. Covington,
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Of counsel.

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[2]These instructions are set forth in the appellant's opening brief, pages 2 and 3, and need not be repeated here.

[3]If this court rejects the appellant's views as to the import of the *Falbo* and *Billings* cases, it should, in any event, reverse the judgment on the ground either that the indictment is defective, or that the evidence demonstrates that the appellant complied with the order, in so far as he is charged in the indictment with having violated it.

The indictment is defective in that it merely charges him with having failed "to report for work of national importance in lieu of induction into the armed forces of the United States." [R. 3.] The indictment does not allege that he refused to submit to induction by declining to proceed to a camp as directed by his local board.

In so far as the limited charge in the indictment is concerned, the evidence demonstrates that the appellant complied with the order. He reported as directed in the order. Upon the specific and limited charge set forth in the indictment, the appellant should have been acquitted. The evidence does not support the verdict or the judgment.

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APPELLEE'S SUPPLEMENTAL BRIEF.

I.

The Appellant Had Not Exhausted the Selective Service Process and Therefore Was Not in a Position to Challenge the Arbitrariness of the Action of the Selective Service Agencies in Not Classifying Him in Class IV-D.

In appellant's reply brief it is claimed that appellant complied with the order of the board in that he appeared at the time and place directed in the board's order; that is, that he appeared at the office of the local board on June 1, 1942. However, he refused to go to the civilian public service camp, as ordered by the local board. [R. 24.]

It is stated in *Falbo v. United States,* 320 U. S. 549, at page 553, referring to any registrant:

> "If he has been classified for military service, his local board orders him to report for induction into the armed forces. If he has been classified a conscientious objector opposed to noncombatant military service, as was petitioner, he ultimately is ordered by the local board to report for work of national importance. In each case the registrant is under the same obligation to obey the order. But in neither case is the order to report the equivalent of acceptance for service. Completion of the functions of the local boards and appellate agencies, important as are these functions, is not the end of the selective service process. The selectee may still be rejected at the induction center and the conscientious objector who is opposed to noncombatant duty may be rejected at the civilian public service camp. Section 3(a) of the Act provides in part that '. . . no man shall be inducted for training and service under this Act unless and until he is acceptable to the land or naval forces for such training and service and his physical and mental fitness for such training and service has been satisfactorily determined . . .' We are informed by the government that pursuant to this section approximately forty per cent of the selectees who report under orders of local boards for induction into the armed forces are rejected, and that, as of October 15, 1943, six hundred and ten of the eight thousand selectees who had reported for civilian work of national importance had been rejected. The connected series of steps into the national service which begins with registration with the local board does not end until the registrant is accepted by the army, navy, or civilian public service camp."

As of October 15, 1943, as is pointed out in the footnote, six hundred and ten of the eight thousand selectees who had reported for civilian work of national importance had been rejected. Had this appellant complied with the board's order and reported at the camp, he might also have been rejected. Therefore, he had not completed the selective service process, as he had not taken the last Step. Consequently, appellant is in error in the contentions made in footnote 3 of appellant's reply brief. The indictment is not defective; the appellant did fail "to report for work of national importance in lieu of induction into the armed forces of the United States"; he simply "reported" at the draft board. The indictment rightfully does not allege that he "refused to submit to *induction*" as "induction was not a requirement under the draft board's order. A registrant is not "inducted" when he reports for work of national importance under civilian direction. Appellant, if he had complied with all of the orders of the board, even to entering the public service camp for duty, would never have been required to come under military authority.

The Government contends that a registrant who is ordered to report for work of national importance must comply with the order of the board and report for work of national importance, and that he may then contest the legality of the order by petitioning for writ of habeas corpus.

Appellee cannot see of what avail the *Billings* case is in this instance. (*Billings v. Truesdell,* decided by the

Supreme Court on March 27, 1944.) Under the law as laid down in that case, a registrant need not submit to military authority in order to put himself in a position to contest the legality of the orders of the board.

The *Falbo* case was concerned with the fate of a conscientious objector classified as IV-E, and ordered to report for work of national importance, as was the appellant in the case at bar; the *Billings* case was concerned with the rights of a registrant classified as 1-A and ordered to report for induction into the armed forces. The *Billings* case has not modified the law enunciated in the *Falbo* case in so far as it applies to a conscientious objector.

There is no doubt but that a selectee should submit to the final order of the draft board. This Honorable Court has so held in *Enge v. Clark,* C. C. A. No. 10367 (June 30, 1944) in the following language:

> "We hold that appellant should have presented himself for induction, where he may have been rejected because of physical or mental unfitness under Section 3(a) of the Act. (See footnote 7, page 553, Falbo v. United States, 320 U. S. 549.) Since he has then exhausted the administrative process, after physical examination and acceptance he 'may then challenge an order (of the Board) in the courts.' Billings v. Truesdell, ... U. S. ....., decided March 27, 1944. If he submit to induction he is not without remedy. He, or someone on his behalf, then may seek to assert the alleged violation of his constitutional or other rights by a petition for writ of habeas corpus addressed to the military commander under whom he is serving."

II.

No Testimony Offered and Stricken by the Trial Court Tended to Prove That Appellant Did Not Have a Fair Hearing.

The testimony ordered stricken was to the effect that the chairman of the local board had stated of Jehovah's Witnesses,

> "I think the organization is rotten, it stinks. The whole organization stinks. It is a disgrace to Christianity. I have no use for it at all." [R. 26, 27.]

This statement was alleged to have been made to a person not a party to, and not in connection with, the classification of the appellant. Had the testimony been admitted, it would not necessarily have shown that the appellant had not been accorded a fair and impartial hearing. The appellant had not required the attendance of the chairman of the draft board at the trial; the chairman had not testified, and had not been confronted with the purported conversation. It is not proper to attempt to establish arbitrary and capricious action on the part of the draft board involving any registrant by the testimony of a witness to statements made by a draft board member outside the draft board offices and not in connection with any particular proceeding or classification concerning such registrant. The substantive defense of the appellant, therefore, was wholly immaterial.

Conclusion.

The appellant was not deprived of his "day in court." The appellant had not exhausted the Selective Service process and was, therefore, not entitled to examine into the actions and mental attitude of the members of the draft board. The judgment of conviction and sentence should be affirmed.

Respectfully submitted,

CHARLES H. CARR,
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No. 10473

United States
Circuit Court of Appeals
For the Ninth Circuit.

BYRON JACKSON CO., a corporation,

Appellant,

vs.

PATTERSON-BALLAGH CORPORATION, a corporation, J. C. BALLAGH and D. G. MILLER,

Appellees.

Transcript of Record
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Upon Appeal from the District Court of the United States for the Southern District of California, Central Division

Rotary Colorprint, 590 Folsom St., San Francisco

No. 10473

United States

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Appellees.

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Upon Appeal from the District Court of the United States for the Southern District of California, Central Division

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*Page numbering appearing at foot of page of original certified Transcript of Record.

In the District Court of the United States, Southern District of California, Central Division.

Civil Action No. 1762-Y

No. 1762-Y

BYRON JACKSON CO., a corporation,

Plaintiff,

vs.

PATTERSON-BALLAGH CORPORATION, a corporation, J. C. BALLAGH and D. G. MILLER,

Defendants.

COMPLAINT

Comes Now the plaintiff, Byron Jackson Co., and for a cause of action against the defendants alleges as follows:

I.

That plaintiff, Byron Jackson Co., is, and at all times herein mentioned was, a corporation organized and existing under and by virtue of the laws of the State of Delaware; that defendant Patterson-Ballagh Corporation is, and at all times herein mentioned was, a corporation organized and existing under and by virtue of the laws of the State of California, with its principal place of business in the County of Los Angeles, State of California, in the Southern District of California, Central Division; that defendants J. C. Ballagh and D. G. Miller both are, and at all times herein mentioned

were, citizens and residents of the County of Los Angeles, State of California, in the Southern District of California, Central Division.

II.

That the jurisdiction of this Court is based upon diversity of citizenship; that this is a suit of a civil nature between [2] citizens of different states, and the amount involved exceeds the sum of Three Thousand Dollars ($3,000), exclusive of interest and costs.

III.

That there are now, and at all times herein mentioned were, one thousand (1,000) shares, and no more, of the capital stock of said defendant Patterson-Ballagh Corporation issued and outstanding, and that of said 1,000 shares 375 are, and at all times herein mentioned were, of record or beneficially owned by the said Ballagh; that of said 1,000 shares 375 are, and at all times since on or about February 15, 1939 were, of record or beneficially owned by the said Miller; and that of said 1,000 shares 250 are, and at all times herein mentioned were, of record or beneficially owned by said plaintiff.

IV.

That at the present time and at all times since February 15, 1939, the Board of Directors of said Patterson-Ballagh Corporation consisted of five (5) persons, and that said five (5) persons are and were at all of said times the said Ballagh, the said Miller, one E. S. Dulin, and other persons who were

selected as such directors by, and in fact were and are representatives of, the said Ballagh and the said Miller upon the said Board. That the said Dulin is, and at all times herein mentioned was, the president of plaintiff and represented and now represents plaintiff upon said Board. That the said Miller is, and at all times since February 15, 1939 was, the president of said Patterson-Ballagh Corporation, and that said Ballagh is, and at all times herein mentioned was, the secretary-treasurer of said Patterson-Ballagh Corporation. That the said Ballagh and the said Miller, by means of their said stock ownership and by means of their said representation upon the Board of Directors of said corporation by themselves and by their said representatives, and by means of [3] their being president and secretary-treasurer respectively of said corporation at all times herein mentioned since February 15, 1939, have dominated, controlled, and directed, and do now dominate, control, and direct each and every of the acts and doings of the said defendant corporation.

V.

That at all times herein mentioned since February 15, 1939, the said Ballagh and the said Miller have fraudulently and unlawfully connived, cooperated, schemed, and conspired, and do now fraudulently and unlawfully connive, cooperate, scheme and conspire, in directing the affairs of the said corporation for their own ends, as distinguished from the well-being of said corporation and the in-

terests of plaintiff as a minority stockholder thereof, and for their own profit as hereinafter in this complaint more particularly set forth.

VI.

That as a part of said scheme and conspiracy said defendants Ballagh and Miller while they along with their said representatives were directors of said defendant corporation, and over the protest of the said Dulin as plaintiff's representative upon said Board, did declare and pay to said Ballagh grossly excessive salaries and compensation for services rendered said corporation, as follows:

That during the calendar year 1939 the said Ballagh was paid the total sum of $15,000 and that said sum was grossly excessive as such salary and compensation in at least the amount of $3,000; that during the calendar year 1940 the said Ballagh was paid the total sum of $30,166.66, and that said sum was grossly excessive as such salary and compensation in at least the amount of $18,166.66; that during the calendar year 1941 and prior to the time of commencing this suit the said Ballagh has been paid [4] the sum of $16,000, and that said sum was grossly excessive as such salary and compensation in at least the sum of $9,000.

VII.

That as a part of said scheme and conspiracy said Ballagh and Miller while they along with their said representatives were directors of said defendant corporation, and over the protest of the said Dulin

as plaintiff's representative upon said Board, did declare and pay to said Miller grossly excessive salaries and compensation for services rendered said corporation, as follows:

That during the calendar year 1940 the said Miller was paid the sum of $19,750, and that said sum was grossly excessive as such salary and compensation in at least the amount of $7,750; that during the calendar year 1941 and prior to the time of commencing this suit the said Miller has been paid the sum of $10,500, and that said sum was grossly excessive as such salary and compensation in at least the amount of $3,500.

VIII.

That plaintiff has at no time since February 15, 1939, received any dividends whatsoever from said Patterson-Ballagh Corporation, and that said excessive salaries and compensation, as hereinbefore set forth, were determined by said Ballagh and Miller in furtherance of the above mentioned scheme and conspiracy, and plaintiff believes and therefore alleges that the amount of said salaries and compensation were fixed with the purpose and intent of depriving the plaintiff of dividends accruing or to accrue to said plaintiff from the said Patterson-Ballagh Corporation. That if said excess of said payments had not been made to the said Ballagh and the said Miller, said excess would have been available for the payment of dividends to the stockholders of said defendant corporation, including

the said plaintiff. That the amounts of said salaries and compensation were neither fairly [5] nor honestly determined by the said Ballagh and the said Miller.

IX.

That for and on account of the payment of said excessive salaries and compensation, as hereinbefore in paragraphs VI and VII of this complaint set forth, said defendants Ballagh and Miller are indebted to said defendant corporation in at least the sum of $41,416.66, no part of which has been repaid by the said Ballagh and the said Miller, or either thereof, to said defendant corporation.

X.

That the plaintiff was a stockholder at the time of each and every transaction of which plaintiff now complains, and that this action is not a collusive one to confer on a court of the United States jurisdiction of any action of which it would not otherwise have jurisdiction.

XI.

That plaintiff has attempted to secure from the directors of said defendant corporation and from the stockholders of said defendant corporation action by said defendant corporation in the bringing and prosecuting of this suit and, to that end, did take the following steps:

(a) That on or about August 5, 1941, plaintiff did serve upon the Board fo Directors of said defendant corporation a demand in words and figures as set forth in Exhibit "A" attached to this com-

plaint, which said Exhibit "A" is by this reference made a part hereof.

(b) That on or about August 8, 1941, said plaintiff did cause the said Dulin, who is and at all times herein mentioned was plaintiff's president and the representative of plaintiff upon the Board of Directors of said defendant corporation, to deliver to the said Miller as president of said defendant [6] corporation a letter in words and figures as set forth in Exhibit "B" attached to this complaint, which said Exhibit "B" is by this reference made a part hereof.

(c) That on or about August 14, 1941, said plaintiff did deliver to each of the stockholders of said defendant corporation, except the said plaintiff, a letter in words and figures as set forth in Exhibit "C" attached to this complaint, which said Exhibit "C" is by this reference made a part hereof, together with a copy of the said demand, Exhibit "A" to this complaint.

XII.

That plaintiff has failed to obtain any action by said directors or said stockholders of said defendant corporation due to the said domination, control, and direction of said defendant corporation by the said Ballagh and the said Miller, and due to said scheme and conspiracy as hereinbefore set forth.

Wherefore, plaintiff prays for a judgment of this Court in favor of said defendant corporation and against said defendants Ballagh and Miller in

the sum of $41,416.66, with interest thereon from the dates of the said respective excess payments of salaries and compensation, and for plaintiff's costs incurred by plaintiff in the commencement and prosecution of this action, and for appropriate attorney's fees for plaintiff's attorneys herein, said costs and attorney's fees to be paid out of such recovery as the defendant corporation may obtain in this action against the said defendants Ballagh and Miller; and that said plaintiff have such other and further relief as may be just.

CHICKERING & GREGORY,
DONALD Y. LAMONT,
LYON & LYON,
LEONARD S. LYON,
IRWIN L. FULLER,
811 W. Seventh Street
Los Angeles, California,
Attorneys for Plaintiff. [7]

EXHIBIT "A"

To the Board of Directors of Patterson-Ballagh Corporation, a California corporation:

Byron Jackson Co., a Deleware corporation, and a stockholder in Patterson-Ballagh Corporation at the present time and at all times herein mentioned, hereby makes demand upon you to commence and prosecute a suit in the name of and on behalf of said Patterson-Ballagh Corporation

against J. C. Ballagh and D. G. Miller on account of the following facts:

1. That said Ballagh and one C. L. Patterson, at all times subsequent to September 20, 1928 and up to on or about February 15, 1939, were the principal stockholders of Patterson-Ballagh Corporation, owning and controlling three-fourths (¾) of the entire capital stock of said corporation, the remaining one-fourth (¼) of such capital stock being owned and controlled by the undersigned; that said Patterson during said time was the president and a director of said Patterson-Ballagh Corporation, and said Ballagh was secretary-treasurer and a director of said Patterson-Ballagh Corporation, and said Ballagh and the said Patterson by said stock ownership controlled, dominated, and directed each and every of the acts of siad Patterson-Ballagh Corporation. That on or about February 15, 1939, said Patterson resigned as president and director of said corporation, and the entire stock owned by said Patterson in said Patterson-Ballagh Corporation was sold to one D. G. Miller by said Patterson; said Miller was thereupon elected president and a director of said corporation on said February 15, 1939, and since that date has been and still is the president and a director of said corporation. That since February 15, 1939, the said Ballagh and the said Miller have connived and cooperated in directing the affairs [8] of said Patterson-Ballagh Corporation, and have at all times since said date dominated, controlled, and directed, and still do domin-

ate, control, and direct each and every of the acts and doings of said Patterson-Ballagh Corporation.

2. That as a part of a scheme and conspiracy said Ballagh and Miller, being in absolute control and domination of said corporation by reason of controlling three-fourths (¾) of the capital stock of said corporation and by reason of controlling the Board of Directors of said corporation, and over the protest of the undersigned, did pay to said Ballagh grossly excessive salaries and compensation for services rendered said corporation, as follows:

That during the calendar year 1939 the said Ballagh was paid the total sum of $15,000, and that said sum was grossly excessive as such salary and compensation in at least the amount of $3,000; that during the calendar year 1940 the said Ballagh was paid the total sum of $30,166.66, and that said sum was grossly excessive as such salary and compensation in at least the amount of $18,166.66; that during the calendar year 1941 and prior to the time of serving this demand, the said Ballagh has been paid the sum of $16,000, and that said sum was grossly excessive as such salary and compensation in at least the amount of $9,000.

3. That as a part of said scheme and conspiracy said Ballagh and Miller, being in absolute control and domination of said corporation by reason of controlling three-fourths (¾) of the capital stock of said corporation and by reason of controlling the Board of Directors of said corporation, and over the protest of the undersigned, did pay to said [9]

Miller grossly excessive salaries and compensation for services rendered said corporation, as follows:

That during the calendar year 1940 the said Miller was paid the sum of $19,750, and that said sum was grossly excessive as such salary and compensation in at least the amount of $7,750; that during the calendar year 1941 and prior to the time of serving this demand the said Miller has been paid the sum of $10,500, and that said sum was grossly excessive as such salary and compensation in at least the amount of $3,500.

4. The undersigned has at no time since February 15, 1939, received any dividends whatsoever from said Patterson-Ballagh Corporation, and the undersigned believes that said excessive salaries and compensation, as hereinbefore set forth, were determined by said Ballagh and said Miller in furtherance of the above mentioned scheme and conspiracy, and with the purpose and intent of depriving the undersigned of dividends accruing or to accrue to the undersigned from the said Patterson-Ballagh Corporation, and that the amounts of said salaries and compensation were neither fairly nor honestly determined by the said Ballagh and the said Miller.

That the undersigned hereby reiterates its demand upon the Board of Directors of said Patterson-Ballagh Corporation that suit be instituted and prosecuted by said Board in the name of and on behalf of the said corporation to collect from the

said Ballagh and the said Miller the amount of all excessive salaries and compensation.

Dated: August 5, 1941.

BYRON JACKSON CO.,
By W. N. BEADLE,
Vice President
By W. H. WIESE,
Secretary [10]

EXHIBIT "B"

August 8, 1941.

D. G. Miller, Esq., President,
Patterson-Ballagh Corporation,
1900 E. 65th St.,
Los Angeles, Calif.

Dear Sir:

Referring to the demand of Byron Jackson Co., bearing the date August 5, 1941, served upon the directors of Patterson-Ballagh Corporation, I, as a director of the last named corporation, urge that said corporation commence and prosecute a suit in accordance with such demand, and that you, as president, and the board of directors take all appropriate action in this regard.

Yours very truly,
(signed) E. S. DULIN.

ESD MJW
By registered mail
return receipt requested. [11]

EXHIBIT "C"

To the Stockholders of Patterson-Ballagh Corporation:

The undersigned, Byron Jackson Co., a stockholder of Patterson-Ballagh Corporation, has heretofore served upon the Board of Directors of the last named corporation a demand, a copy of which is herewith enclosed. Although sufficient time has elapsed since such service, no action has been taken by that Board in accordance with said demand, nor has said Board communicated with the undersigned. Under these circumstances, the undersigned deems it appropriate to appeal, and does hereby appeal, to the stockholders as a body for redress as to the matters contained in said demand and for action by the stockholders in order that compliance may be had with said demand. To this end the undersigned stands ready at all times to cooperate. A reply is requested as to whether you are willing to join with the undersigned in taking whatever legal action may be necessary in order to force Patterson-Ballagh Corporation to proceed in accordance with said demand.

Yours very truly,

BYRON JACKSON CO.

By W. N. BEADLE

Vice President.

Dated: August 14, 1941

[Endorsed]: Filed Sep. 10, 1941 [12]

[Title of District Court and Cause.]

NOTICE OF MOTION TO DISMISS ON BEHALF OF DEFENDANTS AND EACH OF THEM

To the Plaintiff Above Named and Its Attorneys of Record:

You, and Each of You, Will Please Take Notice, that on the 27th day of October, 1941 at the hour of 10:00 o'clock a. m., or as soon thereafter as counsel may be heard, defendants Patterson-Ballagh Corporation, a corporation, J. C. Ballagh and D. G. Miller, and each of them, will move the above entitled court in Courtroom No. 5, Judge Leon R. Yankwich, presiding, located in the Federal Building, Main and Temple Streets, in the City of Los Angeles, State of California, for an order dismissing as to said defendants, and each of them, the complaint herein, on the ground that the court lacks jurisdiction of the subject matter of the complaint, and on the ground that plaintiff has failed to state any claim upon which relief can be granted.

Said motion will be based upon this notice of motion, the points and authorities appended here-

to, and upon the records and files of the above numbered case.

Dated this 9th day of October, 1941.

MUSICK AND BURRELL
By JAMES E. BEDNAR
Attorneys for defendants Patterson-Ballagh Corporation, J. C. Ballagh and D. G. Miller

[Endorsed]: Filed Oct 9, 1941 [13]

At a stated term, to wit: The September Term, A. D. 1941 of the District Court of the United States of America, within and for the Central Division of the Southern District of California, held at the Court Room thereof in the City of Los Angeles on Monday the 27th day of October in the year of our Lord one thousand nine hundred and forty-one.

Present:

The Honorable: Leon R. Yankwich, District Judge.

[Title of Cause.]

No. 1762-Y Civil

ORDER DENYING MOTION TO DISMISS ACTION

This cause coming on for hearing motion of defendant for an order dismissing the action; Donald Y. Lamont, Esq., and Messrs. Lyon and Lyon by

Attorney Lyon appearing as counsel for the plaintiff; James E. Bednar, Esq., appearing as counsel for the defendants:

Attorney Bedner presents motion of defendants to dismiss the action; Attorney Lamont replies to motion; Attorney Bednar argues in rebuttal; and it is ordered that the motion be, and it is, denied, twenty days being allowed to the defendants to answer.

23/160 [14]

[Title of District Court and Cause]

ANSWER TO COMPLAINT

Come now defendants Patterson-Ballagh Corporation, a corporation, J. C. Ballagh and D. G. Miller, severally, and each of said defendants, in answer to the complaint on file herein, admits, denies and alleges as follows:

I.

Defendants admit all allegations of paragraph I of said complaint except that defendants deny that D. G. Miller has at all times mentioned therein been a citizen and resident of the County of Los Angeles, State of California, and in this connection defendants allege that said Miller is now and at all times mentioned in said paragraph I has been a citizen and resident of the [15] County of Los Angeles, State of California, except for a period

of approximately two and one-half years, extending from approximately the month of April, 1936, to approximately the month of October, 1938, during which period of approximately two and one-half years said Miller was at all times a citizen and resident of the County of San Joaquin, State of California.

II.

Answering paragraph II of said complaint, defendants admit that the jurisdiction of this court must, if present, be based upon diversity of citizenship, that this is a suit of a civil nature, that the amount involved exceeds the sum of $3,000 exclusive of interest and costs, but defendants deny generally, specifically, and positively each and every other allegation therein contained, and every part thereof, which has not been heretofore specifically admitted in paragraph II of this answer, and particularly deny that the alleged and requisite diversity of citizenship is present.

III.

Answering paragraph III of said complaint, defendants admit that there is now, and that there has been at all times subsequent to September 20, 1928, a total of 1,000 shares of the capital stock of defendant Patterson-Ballagh Corporation issued and outstanding; admit that plaintiff now owns and controls, and has at all times subsequent to September 20, 1928, owned and controlled 250 shares of the capital stock of defendant Patterson-Ballagh Corporation, constituting one-fourth of its total is-

sued and outstanding capital stock; admit that from September 20, 1928, to on or about August 8, 1931, the remainder of defendant Patterson-Ballagh Corporation's issued and outstanding capital stock was beneficially owned and controlled as follows: 375 shares by J. C. Ballagh and 375 by C. L. Patternson; admit that from on or about August 8, 1931, to on or about February 15, 1939, said [16] remainder was beneficially owned and controlled as follows: 375 shares by C. L. Patterson, 125 shares by J. C. Ballagh and 250 shares by Highland Investment Corporation, Ltd., a corporation; admit that from on or about February 15, 1939, up to and including the present time said remainder has been and is now beneficially owned and controlled as follows: 125 shares by defendant J. C. Ballagh, 250 shares by Highland Investment Corporation, Ltd., a corporation, and 375 shares by defendant D. G. Miller; admit that at all times since September 20, 1928, up to and including the present time, the status of the record ownership of all of the issued and outstanding shares of defendant Patterson-Ballagh Corporation has been the same as the status of the beneficial ownership and control of said shares as hereinbefore alleged in paragraph III of this answer, with one exception, to wit: the 375 shares beneficially owned and controlled by defendant D. G. Miller from on or about February 15, 1939, up to and including the present time have during all of said times stood and now stand in the name of C. L. Patterson as the record owner thereof.

IV.

Answering paragraph IV of said complaint, defendants admit that from on or about February 15, 1939, to on or about June 27, 1939, the Board of Directors of defendant Patterson-Ballagh Corporation was composed of five persons, to wit, J. C. Ballagh, D. G. Miller, E. S. Dulin, H. C. Armington and H. W. Elliott; admit that from on or about June 27, 1939, up to and including the present time, the Board of Directors of defendant Patterson-Ballagh Corporation has been and is now composed of five persons, to wit, J. C. Ballagh, E. S. Dulin, D. G. Miller, H. C. Armington and Howard Burrell; admit that E. S Dulin is now and at all times mentioned in the complaint has been the [17] President of plaintiff and that said Dulin has at all times represented and now represents plaintiff upon said Board; admit that D G. Miller is now and at all times since February 15, 1939, has been President of Patterson-Ballagh Corporation, and that J. C. Ballagh is now and at all times since February 15, 1939, has been Secretary and Treasurer of Patterson-Ballagh Corporation.

Further answering said paragraph IV defendants deny generally, specifically, and positively each and every allegation therein contained, and every part thereof, which has not been heretofore specifically admitted in paragraph IV of this answer.

V.

Answering paragraph V of said complaint, defendants deny generally, specifically, and positively

each and every allegation therein contained, and every part thereof.

VI.

Answering paragraph VI of said complaint, defendants admit that during the year 1939 defendant Patterson-Ballagh Corporation paid to defendant J. C. Ballagh as compensation for services rendered by said Ballagh to and for said corporation during said year, the sum of $15,000; admit that during the calendar year 1940 defendant Patterson-Ballagh Corporation paid to defendant J. C. Ballagh as compensation for services rendered by said Ballagh to and for said corporation during said year, the sum of $30,166.66, and that E. S. Dulin objected to the payment of $10,000 of said sum; admit that during the calendar year 1941 and prior to the filing of the complaint herein, defendant Patterson-Ballagh Corporation paid to defendant J. C. Ballagh as compensation for services rendered by said Ballagh to and for said corporation during said time, the sum of $16,000, and that E. S. Dulin objected to the payment of $7,000 of said sum. [18]

Further answering said paragraph VI, defendants deny generally, specifically, and positively each and every allegation therein contained, and every part thereof, which has not been heretofore specifically admitted in paragraph VI of this answer.

VII.

Answering paragraph VII of said complaint, defendants admit that during the calendar year 1940, defendant Patterson-Ballagh Corporation paid to

defendant D. G. Miller as compensation for services rendered by said Miller to and for said corporation during said year, the sum of $19,750; admit that during the calendar year 1941 and prior to the filing of the complaint herein, defendant Patterson-Ballagh Corporation paid to defendant D. G. Miller as compensation for services rendered by said Miller to and for said corporation during said time, the sum of $10,500.

Further answering said paragraph VII, defendants deny generally, specifically, and positively, each and every allegation therein contained, and every part thereof, which has not been heretofore specifically admitted in paragraph VII of this answer.

VIII.

Answering paragraph VIII of said complaint, defendants admit that Patterson-Ballagh Corporation has paid no dividends on any of its issued and outstanding shares since February 15, 1939, but deny generally, specifically, and positively each and every allegation therein contained, and every part thereof, which has not been heretofore specifically admitted in paragraph VIII of this answer.

IX.

Defendants deny generally, specifically, and positively each and every allegation contained in paragraph IX of said complaint, and every part thereof. [19]

X.

Answering paragraph X of said complaint, defendants admit that plaintiff is now, and ever since

on or about September 20, 1928, has been, a stockholder of defendant Patterson-Ballagh Corporation, but deny generally, specifically, and positively each and every allegation therein contained, and every part thereof, which has not heretofore been specifically admitted in paragraph X of this answer.

XI.

Answering paragraph XI of said complaint, defendants admit that on or about August 5, 1941, they received a communication, purportedly from plaintiff, in words and figures as set forth in Exhibit A attached to the complaint; admit that on or about August 8, 1941, E. S. Dulin delivered to defendant Patterson-Ballagh Corporation a communication in words and figures as set forth in Exhibit B attached to the complaint and that said E. S. Dulin is now, and at all times mentioned in the complaint, since June 13, 1930, has been, plaintiff's President and the representative of plaintiff upon the Board of Directors of defendant Patterson-Ballagh Corporation; admit that on or about August 14, 1941, defendants Ballagh and Miller received through the mail a communication in words and figures as set forth in Exhibit C attached to the complaint, together with a communication in words and figures as set forth in Exhibit A attached to the complaint.

Further answering each and all of the allegations of paragraph XI of said complaint, which have not been heretofore specifically admitted in paragraph XI of this answer, defendants have no information

or belief upon the subject sufficient to enable them to answer said allegations, and placing their denial on that ground, defendants deny generally, specifically, and [20] positively each and every allegation contained in paragraph XI of said complaint, and every part thereof, which has not been heretofore specifically admitted in paragraph XI of this answer.

XII.

Defendants deny generally, specifically, and positively each and every allegation contained in paragraph XII of said complaint, and every part thereof.

Wherefore, defendants pray:

(1) That plaintiff take nothing by reason of the complaint on file herein;

(2) That defendants recover their costs of suit incurred herein;

(3) For such other and further relief as may appear just and equitable to the court.

MUSICK AND BURRELL
HOWARD BURRELL
Attorneys for defendants

(Affidavit of Service by Mail)

[Endorsed]: Filed Nov. 28, 1941. [21]

At a stated term, to wit: The February Term, A. D. 1942 of the District Court of the United States of America, within and for the Central Di-

vision of the Southern District of California, held at the Court Room thereof, in the City of Los Angeles on Thursday the 2nd day of July in the year of our Lord one thousand nine hundred and forty-two.

Present:

The Honorable: Dave W. Ling, District Judge

[Title of Cause.]

No. 1762-Y Civil

TRIAL

This cause coming on for hearing; Donald Y. Lamont, Esq., of the law firm of Messrs Chickering and Gregory of San Francisco, California, appearing as counsel for the plaintiff; and Messrs. Musick and Burrell by J. E. Bednar, Esq., appearing as counsel for the defendants; and C. W. McClain, Court Reporter, being present and reporting the testimony and the proceedings:

Attorneys Bednar and Lamont, respectively, make statements. Attorney Bednar files amendment to answer. Attorney Lamont makes opening statement of facts to the Court in behalf of the plaintiff, and Attorney Bednar makes a statement to the Court. The following exhibits are offered and admitted into evidence:

Plf's Ex. 1—Copies of minutes A-1, appearing in Appendix to depositions of Ballagh and Miller, filed June 29, 1942.

Plf's Ex. 2—Five (5) sheets showing salaries, etc., Patterson Ballagh corp., et al.

Plf's Ex. 3—Number of sheets, dividends paid to J. C. Ballagh and C. L. Patterson, Byron Jackson Co., salaries, etc., and dividends paid to Schurman and Dulin.

Plf's Ex. 4—One (1) sheet—sales. [22]

Plf's Ex. 5-a—Audit report, 11/30/39, Patterson-Ballagh Corp.

Plf's Ex. 5-b—Audit report, 11/30/40, Patterson-Ballagh Corp.

Plf's Ex. 5-c—Audit report, 11/30/41, Patterson-Ballagh Corp.

Plf's Ex. 6-a—Folder—balance sheet, 12/31/38, Patterson-Ballagh Corp.

Plf's Ex. 6-b—Statement of assets and liabilities, 11/30/40, Patterson-Ballagh Corp.

Plf's Ex. 6-c—Statement of assets and liabilities, 12/31/40, Patterson-Ballagh Corp.

Plf's Ex. 7—Letter, 2 pages, 1/23/42, to J. C. Ballagh, etc., from Joseph "H" Pennington.

Plf's Ex. 8—Letter, 2/1/37, to J. C. Ballagh from Dulin.

Plf's Ex. 9—Letter, 3/23/37, to C. L. Patterson, President from Dulin.

Plf's Ex. 10—Telegram, 9/25/38, to Patterson-Ballagh Corp. from C. S. Dulin.

Plf's Ex. 11—Copy of letter, 7/20/39, to Patterson-Ballagh Corp., from.....

Plf's Ex. 12—Letter, 9/8/39, to Patterson-Ballagh Corp. from Dulin.

Plf's Ex. 13—Letter, 2/25/41, to D. G. Miller, President, from Dulin.

Plf's Ex. 14—Letter to Patterson-Ballagh Corp. from Dulin, 6/25/41.

Plf's Ex. 15-a—Agreement between Byron Jackson Pump Co. to Patterson, etc., 9/20/28.

Plf's Ex. 15-b—Agreement between Patterson-Ballagh Corp. and Jackson, etc., 9/20/28.

Plf's Ex. 15-c—Agreement between Byron Jackson Pump Co. and Patterson, etc., 9/20/28.

Plf's Ex. 15-d—Agreement between Patterson, et al., and Byron Jackson Pump Co., 9/20/28.

At 11:55 A. M. court recesses until 2 P. M. At 2 P. M. court reconvenes and all being present as before, the Court orders that the trial proceed. The following exhibit is offered and admitted into evidence:

Plf's Ex. 16—Copy of 3 page letter, 6/29/39, to Byron Jackson Co. from Patterson-Ballagh Corp. [23]

J. C. Ballagh, at 2:10 P. M., is called, sworn, and testifies for the plaintiff on direct examination by Attorney Lamont. There is no cross-examination of this witness. The following exhibits are either offered and admitted into evidence or marked for identification, as indicated:

Deft's Ex. A—Chart, gross annual sales, etc.

Deft's Ex. B—Chart, sale of lip protectors, etc.

Deft's Ex. C for Ident.—Non-lip protector.

Deft's Ex. D for Ident.—Lip protector.

Deft's Ex. E—Catalogue of Patterson Ballagh.

Deft's Ex. F—Chart, cumulative dollar return on investment.

At 3:17 P. M. court recesses. At 3:25 P. M. court

reconvenes and all being present as before, J. C. Ballagh resumes the stand and testifies further on direct examination by Attorney Lamont, and there is no cross-examination. The following exhibits are offered and admitted into evidence:

Deft's Ex. G—Chart indicating year by year increase in dollar sales.

Deft's Ex. H—Copy of patent, No. 2,272,395, to James C. Ballagh.

De Mont George Miller, at 3:43 P. M., is called, sworn, and testifies for the plaintiff on direct examination by Attorney Lamont, and at 4:23 P. M., on cross-examination by Attorney Bednar. The following exhibits are offered and admitted into evidence:

Plf's Ex. 17-a—Copy of patent 2,285,742 to De-Mont G. Miller.

Plf's Ex. 17-b—copy of patent 2,239,159 to De-Mont G. Miller.

Plf's Ex. 18-a—Graph-distribution of profits, etc.

Plf's Ex. 18-b—Graph-percentage of profits.

Plf's Ex. 18-c—Graph-comparison of executive salaries.

Plf'd Ex. 18-d—Graph-distribution of corporate payments, etc.

At 4:30 P. M. the Court declares a recess in the trial of this cause until 10 A. M., July 3, 1942. 28/272 [24]

[Title of District Court and Cause.]

AMENDMENT TO ANSWER

Permission of the court having been first obtained, defendants Patterson-Ballagh Corporation, a corporation, J. C. Ballagh and D. G. Miller, severally, and each of said defendants, hereby amend their answers on file herein by adding thereto the following allegations:

I.

At all times mentioned in the complaint one E. S. Dulin was the duly appointed and acting agent of plaintiff and was acting within the scope of his authority.

II.

On January 21, 1941, an annual meeting of shareholders of defendant was duly and regularly held at which there were [25] present in person or by proxy all of the shareholders of defendant corporation including said E. S. Dulin, who, at that time represented not only the one share standing in his name but also the two hundred forty-nine (249) shares standing in the name of plaintiff.

III.

At said annual meeting of shareholders J. C. Ballagh nominated H. C. Armington, J. C. Ballagh, Howard Burrell, E. S. Dulin and D. G. Miller to serve as directors during the ensuing year or until the election and appointment of their successors. After said nominations it was moved by

J. C. Ballagh, seconded by E. S. Dulin, and unanimously carried that the nominations be closed and that the Secretary of the corporation be instructed to cast a ballot on behalf of all shareholders present in person or by proxy for and in favor of the persons nominated as directors as aforesaid. The Secretary thereupon cast said ballot and said nominees were duly elected directors for the ensuing year or until election or appointment of their successors.

IV.

On January 21, 1941, following the meeting of shareholders hereinbefore set forth, there was duly and regularly held a meeting of the Board of Directors of defendant corporation, at which all directors including said E. S. Dulin were present. At said meeting H. C. Armington nominated the following persons for the following offices:

For President—D. G. Miller
For Secretary and Treasurer—J. C. Ballagh
For Assistant Secretary and Assistant Treasurer—M. G. Nolan. [26]

There were no further nominations, and on motion of H. C. Armington, seconded by Howard Burrell, and unanimously carried by the vote of all persons including said E. S. Dulin, it was resolved that the nominations be closed and that the persons nominated as officers for the year be elected and appointed as such by acclamation.

V.

Prior to the election of said directors as aforesaid and prior to the election of said officers as aforesaid, said E. S. Dulin, representing plaintiff herein, had no notice or knowledge that the attitude of the remaining directors in respect to the matters of compensation complained of in the complaint would be any different for the ensuing year of 1941 from their attitude concerning the same for the preceding year of 1940. Prior to the election of said directors and officers said E. S. Dulin, representing plaintiff, had full knowledge of the attitude of the remaining directors and of the officers in respect to the matters of compensation complained of in the complaint.

VI.

By reason of the foregoing plaintiff has waived any right that it might have to complain of the matters set forth in the complaint herein.

Respectfully submitted,

MUSICK AND BURRELL
HOWARD BURRELL
Attorneys for defendants

[Endorsed]: Filed July 2, 1942. [27]

[Title of District Court and Cause.]

VERIFICATION OF COMPLAINT

State of California
County of Los Angeles—ss.

E. S. Dulin, being first duly sworn, deposes and says that he is and at all times mentioned in the complaint in the above entitled action was the President of Byron Jackson Co., a Delaware corporation, and makes this verification for and on behalf of said corporation; that he has read the complaint in the above entitled action and knows the contents thereof and that the same is true of his own knowledge.

E. S. DULIN

Subscribed and sworn to before me this 3rd day of July, 1942.

[Seal] IRENE J. KNUDSEN
Notary Public in and for said County and State.

[Endorsed]: Filed Jul 3, 1942 [28]

At a stated term, to wit: The February Term, A. D. 1942 of the District Court of the United States of America, within and for the Central Division of the Southern District of California, held at the Court Room thereof, in the City of Los Angeles

on Friday the 3rd day of July in the year of our Lord one thousand nine hundred and forty-two.

Present:

The Honorable: Dave W. Ling, District Judge

[Title of Cause.]

No. 1762-YY Civil

This cause coming on for further trial without a jury; Donald Y. Lamont, Esq., appearing as counsel for the plaintiff; Messrs. Musick and Burrell by James E. Bednar, Esq., appearing as counsel for the defendants; and C. W. McClain, Court Reporter, being present and reporting the proceedings:

E. S. Dulin, at 9:58 A.M., is called, sworn, and testifies for the plaintiff on direct examination by Attorney Lamont, and at 10:32 A.M., is cross-examined by Attorney Bednar.

At 10:57 A.M. court recesses. At 11:06 A.M. court reconvenes and all being present as before, E. S. Dulin resumes the stand and testifies further on cross-examination by Attorney Bednar, on redirect examination by Attorney Lamont, and on recross-examination by Attorney Bednar. The following exhibit is offered and admitted into evidence:

Defts' Ex. I—Letter, 3/27/40, to Howard Burrell from E. S. Dulin

E. S. Bunch, at 11:30 A.M., is called, sworn, and testifies for the plaintiff on direct examination by Attorney Lamont, and is examined on voir dire by Attorney Bednar. [29]

John D. Chesnut, at 11:46 A.M., is called, sworn,

and testifies for the plaintiff on direct examination by Attorney Lamont.

At 11:50 A.M. the plaintiff rests.

Howard Burrell, at 11:52 A.M., is called, sworn, and testifies for the defendant on direct examination by Attorney Bednar.

At 12:07 P.M. court recesses until 2 P.M. At 2 P.M. court reconvenes and all being present as before, the following exhibit is offered and admitted in evidence:

Plf's Ex. 19—Two (2) sheets containing executive salaries, etc.

Howard Burrell, heretofore sworn, resumes the stand and testifies further on direct examination by Attorney Bednar, and at 2:20 P.M. on cross-examination by Attorney Lamont.

Ray Walden Morris, at 2:46 P.M., is called, sworn, and testifies for the defendant on direct examination by Attorney Bednar and at 3:03 P.M. on cross-examination by Attorney Lamont. The following exhibit is offered and admitted in evidence:

Defts' Ex. J—Photograph.

At 3:15 P.M. court recesses. At 3:27 P.M. court reconvenes and all being present as before, J. C. Ballagh, heretofore sworn, resumes the stand and testifies for the defendants on direct examination by Attorney Bednar. The following exhibits are offered and admitted in evidence:

Defts' Ex. K-1 to K-9 inclusive—Each being a photograph.

Defts' Ex. L—Copy of agreement, 7 pages, 10/8/40, between Bettis Rubber Co., Ltd., and Patterson-Ballagh Corp.

At 4:30 P.M. the Court declares a recess in the trial of this cause until July 6, 1942.

28/291 [30]

At a stated term, to wit: The February Term, A. D. 1942 of the District Court of the United States of America, within and for the Central Division of the Southern District of California, held at the Court Room thereof, in the City of Los Angeles on Monday the 6th day of July in the year of our Lord one thousand nine hundred and forty-two.

Present:

The Honorable: Dave W. Ling, District Judge

[Title of Cause.]

No. 1762-Y Civil

This cause coming on for further non-jury trial; Donald Y. Lamont, Esq., appearing as counsel for the plaintiff; Messrs. Musick and Burrell by James E. Bednar, Esq., appearing as counsel for the defendants; and C. W. McClain, Court Reporter, being present and reporting the testimony and the proceedings:

J. C. Ballagh, heretofore sworn, continues testimony on direct examination by Attorney Bednar. The following exhibits are either offered and admitted in evidence or marked for identification, as indicated:

Defts' Ex. M—Photos of pipe wiper on circular (printed matter excluded).

Defts' Ex. N for ident.—Tubing protector.

At 11:10 A.M. court recesses. At 11:20 A.M. court reconvenes, and all being present as before, J. C. Ballagh continues testimony on direct examination by Attorney Bednar. The following exhibit is offered and admitted in evidence:

Defts' Ex. O—Photo of sucker rod wiper.

J. C. Ballagh testifies on cross-examination by Attorney Lamont. [31]

At 11:50 A.M. court recesses until 2 P.M.

John M. Grant, at 2 P.M., is called, sworn, and testifies for the plaintiff on direct examination by Attorney Lamont, on voir dire by Attorney Bednar, and at 2:14 P.M., on cross-examination by Attorney Bednar.

Walter H. Wiese, at 2:20 P.M., is called, sworn, and testifies for the plaintiff on direct examination by Attorney Lamont and on cross-examination by Attorney Bednar. The following exhibit is offered and admitted in evidence:

Plf's Ex. 20—Copy of Hopkins patent #1,619,728.

J. C. Ballagh, heretofore sworn, resumes the stand at 2:26 P.M. and testifies further on examination by Attorney Lamont, and at 2:53 P.M. on cross-examination by Attorney Bednar.

John D. Chesnut, heretofore sworn, resumes the stand at 2:56 P.M. and testifies on direct examination by Attorney Lamont. The following exhibits are offered and admitted by the plaintiff:

Plf's Ex. 21—Copy of Berryman patent, 1,913,018

Plf's Ex. 22—Copy of Bettis patent, 2,166,937

Plf's Ex. 23—Copy of Smith patent, 2,197,531

Plf's Ex. 24—Copy of Conrader patent, 831,143

Plf's Ex. 25—Copy of Penfield, et al., patent 2,215,377

Plf's Ex. 26—Copy of Ballagh patent, 2,272,395

Plf's Ex. 27—Copy of Woods patent, 1,764,769.

At 3:24 P.M. court recesses. At 3:35 P.M. court reconvenes and all being present as before:

The plaintiff rests. No further evidence is offered for the defendants.

At 3:40 P.M. it is ordered that this case be, and it hereby is, continued to July 7, 1942, at 10 A.M., for further trial.

28/324 [32]

At a stated term, to wit: The February Term, A. D. 1942 of the District Court of the United States of America, within and for the Central Division of the Southern District of California, held at the Court Room thereof, in the City of Los Angeles on Tuesday the 7th day of July in the year of our Lord one thousand nine hundred and forty-two.

Present:

The Honorable: Dave W. Ling, District Judge

[Title of Cause.]

No. 1762-Y Civil

This cause coming on for further hearing without

a jury; Donald Y. Lamont, Esq., appearing as counsel for the plaintiff; Messrs. Musick and Burrell by James E. Bednar, Esq., appearing as counsel for the defendants; and C. W. McClain, Court Reporter, being present and reporting the proceedings:

Attorney Lamont argues. At 10:54 A.M. court recesses. At 11:03 A.M. court reconvenes, and all being present as before, Attorney Bednar argues.

At noon court recesses until 2 P.M. At 2 P.M. court reconvenes herein and all being present as before, Attorney Bednar argues further. At 2:16 P.M. Attorney Lamont argues further.

It is ordered that the cause be submitted.

28/340 [33]

[Title of District Court and Cause.]

NOTICE OF HEARING OF MOTION TO REOPEN CASE TO ADMIT NEWLY DISCOVERED EVIDENCE

To the Plaintiff Above Named, and to Chickering & Gregory, Donald Y. Lamont, Lyon & Lyon, Leonard S. Lyon and Irwin L. Fuller, Its Attorneys:

You and Each of You Will Please Take Notice that on Monday, the 17th day of August, 1942, in the Courtroom of the above entitled Court in the Federal Building, Los Angeles, California, at 10:00 O'clock in the forenoon of said day, or as soon thereafter as the same may be heard, defendants, and each of them, will bring on for hearing their an-

nexed petition for reopening the case to admit newly discovered evidence.

Dated: July 31, 1942.

MUSICK AND BURRELL
HOWARD BURRELL
Attorneys for Defendants [34]

[Title of District Court and Cause.]

PETITION FOR REOPENING CASE TO ADMIT NEWLY DISCOVERED EVIDENCE

Come now the defendants Patterson-Ballagh Corporation, a corporation, J. C. Ballagh and D. G. Miller, and each of them, by their attorneys and show to the Court:

Upon the trial of the above entitled cause, which commenced on or about July 1, 1942, and continued through July 7, 1942, defendants, and each of them, introduced into evidence the following facts:

(1) That defendant D. G. Miller had invented a certain [35] open hole tool joint protector, had applied for patents thereon, and had assigned all patent rights in and to the same to the defendant corporation, royalty free, and that the United States Patent Office had at the time of trial allowed two claims in reference to the patent application pending in reference to said device;

(2) That defendant J. C. Ballagh had invented a certain lip protector for drill pipe, had applied for patents thereon, and had assigned all patent

rights in and to the same to the defendant corporation, royalty free, but that at the time of trial no claims had been allowed upon the same, either by the United States Patent Office or the patent office of any other foreign nation.

In rebutting the foregoing evidence, plaintiff introduced evidence indicating that the patentability of the foregoing mentioned devices was doubtful.

Since the trial and submission of the case, defendants, and each of them, have for the first time received notice of the fact that the Dominion of Canada has granted and allowed patents on both of the foregoing mentioned devices.

Attached hereto and marked Exhibit 1 and hereby incorporated herein is a copy of a letter from the patent attorneys of defendant, who also happen to be one of the attorneys of record for the plaintiff herein, dated May 12, 1942, indicating that applications for patents in respect to the devices in question were filed in Canada on or about April 16, 1941.

Attached hereto marked Exhibit 2 is a true and exact copy of an assignment executed April 10, 1941, by defendant J. C. Ballagh, assigning to the defendant corporation any and all patent rights which might be granted in Canada in respect to the device referred to at the trial of this action as the lip protector. [36]

Attached hereto marked Exhibit 3 is a true and exact copy of an assignment executed April 10, 1941, by defendant D. G. Miller, assigning to the defendant corporation any and all patent rights which

might be granted in Canada in respect to the device referred to at the trial of this action as the open hole tool joint protector.

Attached hereto marked Exhibits 4-a and 4-b and hereby incorporated herein are true and exact copies of letters written July 7, 1942, by the patent attorneys of the defendant corporation, and received by defendants July 8, 1942, notifying defendants, and each of them, for the first time that the two patent applications in Canada in respect to the open hole tool joint protector and the lip protector had been officially allowed by the Canadian Patent Office.

Attached hereto marked Exhibits 5-a and 5-b, and hereby incorporated herein, are copies of the original notices of allowance issued by the Canadian Patent Office in respect to the applications for patent upon the aforementioned lip protector and upon the aforementioned open hole tool joint protector respectively.

The newly discovered evidence, to wit, the notices of allowance from the Canadian Patent Office, indicate that, contrary to the evidence and contentions of plaintiff, the two devices in question are plainly patentable.

The newly discovered evidence, to wit, the allowance of patent by the Canadian Patent Office upon the two devices hereinbefore mentioned was not brought to the attention of the defendants, or any of them, until after the above entitled case had been tried and the case submitted, as more fully appears from the affidavit of James E. Bednar, at-

tached hereto as Exhibit 6, and hereby incorporated herein.

Wherefore, defendants, and each of them, move this Court [37] for an order reopening this case and receiving in evidence upon the hearing of this motion, the originals of the exhibits attached hereto and authorizing defendants to substitute true and exact copies in the record for said originals.

Upon the hearing of this motion defendants will read and refer to the papers and pleadings on file in this case, and as points and authorities will rely upon the following:

> Reopening Case Because of Newly Discovered Evidence Is Proper. Walker on Patents (Deller's Ed.) Vol. 4, Sec. 902A and cases cited.
>
> Reopening Case Is Addressed to Discretion of the Court. Walker on Patents (Deller's Ed.) Vol. 4, Sec. 902A and cases cited.

Dated this 31st day of July, 1942.

MUSICK AND BURRELL
HOWARD BURRELL
Attorneys for defendants

Good Cause Appearing Therefor, It Is Ordered that the time of service of the foregoing notice of hearing and petition for reopening is so shortened that service thereof upon the attorneys for plaintiff prior to 5:00 P.M. on the day of Au-

gust, 1942, is adjudged to be sufficient notice of the proceedings mentioned therein.

Dated: this day of August, 1942.

.....

Judge of the District Court

[38]

EXHIBIT 1

Law Offices
Lyon & Lyon
Patent and Trademark Causes
811 West Seventh Street
Los Angeles

May 12, 1941

Patterson-Ballagh Corporation
1900 East 65th Street
Los Angeles, California

Attention Mr. James C. Ballagh

Gentlemen:

Re: Canadian Patent Applications
Our docket Nos. 51/18-19

This is to advise you of the filing of the above applications as follows:

51/18

James C. Ballagh Filed Apr. 16, 1941 Ser. No. 482127

51/19

DeMont G. Miller Filed Apr. 16, 1941 Ser. No. 482128

We enclose copies of the applications as filed, and will keep you advised of further developments.

Very truly yours,
LYON & LYON

L. B.
Enc

[Endorsed]: Deft. Exhibit No. 28. Filed 8/17, 1942. Edmund L. Smith, Clerk. By J. M. Horn, Deputy Clerk. [39]

EXHIBIT 2

51/18

ASSIGNMENT

In consideration of one dollar to me paid by Patterson-Ballagh Corporation of the City of Los Angeles, State of California, I do hereby sell and assign to the said Patterson-Ballagh Corporation all my right, title and interest in and to my invention for new and useful improvements in Protector for Drill Pipe as fully set forth and described in the specification which I have signed preparatory to obtaining a patent in Canada; and I do hereby authorize and request the Commissioner of Patents to issue the said patent to the said Patterson-Ballagh Corporation in accordance with this assignment.

Witness my hand and seal this 10 day of April, 1941, at the City of Los Angeles, State of California.

JAMES COURTENAY BALLAGH. [40]

51/18

State of California,
County of Los Angeles,
United States of America,—ss.

I, Howard Coleman Armington of Los Angeles, in the County of Los Angeles, State of California, United States of America, make oath and say:

1. That I was personally present and did see James Courtenay Ballagh, named in the attached assignment, who is personally known to me to be the person named thereon, duly sign and execute the same for the purpose named thereon.

2. That I am the subscribing witness to the said assignment.

HOWARD COLEMAN ARMINGTON

Sworn to Before Me at Los Angeles, in the County of Los Angeles, State of California, United States of America, this 10 day of April, 1941.

(Seal) MAY G. NOLAN,
Notary Public in and for the County of Los Angeles, State of California. My Commission Expires March 7, 1943.

[Endorsed]: Deft. Exhibit No. 29. Filed 8/17, 1942. Edmund L. Smith, Clerk. By J. M. Horn, Deputy Clerk. [41]

EXHIBIT 3

51/19

ASSIGNMENT

In consideration of one dollar to me paid by Patterson-Ballagh Corporation of the City of Los Angeles, State of California, United States of America, I do hereby sell and assign to the said Patterson-Ballagh Corporation all my right, title and interest in and to my invention for new and useful improvements in Open Hole Tool Joint Protectors, as fully set forth and described in the specification which I have signed preparatory to obtaining a patent in Canada; and I do hereby authorize and request the Commissioner of Patents to issue the said patent to the said Patterson-Ballagh Corporation in accordance with this assignment.

Witness my hand and seal this 10 day of April, 1941, at the City of Los Angeles, State of California, United States of America.

DeMONT GEORGE MILLER

[42]

51/19

State of California,
County of Los Angeles,
United States of America—ss:

I, Howard Coleman Armington, of Los Angeles, in the County of Los Angeles, State of California, United States of America, make oath and say:

1. That I was personally present and did see DeMont George Miller, named in the attached assignment, who is personally known to me to be the person named thereon, duly sign and execute the same for the purpose named thereon.

2. That I am the subscribing witness to the said assignment.

HOWARD COLEMAN ARMINGTON.

Sworn to Before Me at Los Angeles, in the County of Los Angeles, State of California, United States of America, this 10 day of April, 1941.

(Seal) MAY G. NOLAN,
Notary Public in and for the County of Los Angeles, State of California. My Commission Expires March 7, 1943.

[Endorsed]: Deft. Exhibit No. 30. Filed 8/17, 1942. Edmund L. Smith, Clerk. By J. M. Horn, Deputy Clerk. [43]

EXHIBIT 4-a

Law Offices
Lyon & Lyon
Patent and Trademark Causes

811 West Seventh Street
Los Angeles

July 7, 1942.

Patterson-Ballagh Corporation,
1900 East 65th Street
Los Angeles, California.

Gentlemen:

Re: Canadian Patent Application

Serial No. 482128 on "Open Hole Tool Joint Protector"—DeMont G. Miller.

We are pleased to advise you that the above identified Canadian Patent application was officially allowed by the Canadian Patent Office on June 23, 1942.

The final Government fee of $20.00 must be paid not later than six months from the date of allowance, or by December 23, 1942. To this amount must be added $2.50 for the charge of our Canadian associate for making the payment into the Patent Office and receiving and forwarding the patent to us.

Please let us have your instructions and remittance for $22.50 at such time as you wish the patent to issue, and in any event not later than December

10, 1942, so that the same may reach the Canadian Patent Office in sufficient time.

Yours very truly,

IJK LYON & LYON

[Endorsed]: Deft. Exhibit No. 31. Filed 8/17 1942. Edmund L. Smith, Clerk. By J. M. Horn, Deputy Clerk. [44]

EXHIBIT 4-b

Law Offices
Lyon & Lyon
Patent and Trademark Causes
811 West Seventh Street
Los Angeles

July 7, 1942.

Patterson-Ballagh Corporation,
1900 East 65th Street
Los Angeles, California.

Gentlemen:

Re: Canadian Patent Application
Serial No. 482127 on "Protector for Drill Pipe"—J. C. Ballagh

We are pleased to advise you that the above identified application was officially allowed by the Canadian Patent Office June 23, 1942.

The final Government fee of $20.00 must be paid not later than six months from the date of allow-

ance, or by December 23, 1942. To this amount must be added $2.50 to cover our Canadian associate's charge for making the payment into the Patent Office in Canada and receiving and forwarding the patent to us.

Please let us have your instructions and remittance at such time as you wish the patent to issue and in any event not later than December 10, 1942 so that the same may reach the Canadian Patent Office in sufficient time.

Yours very truly,

IJK LYON & LYON.

[Endorsed]: Deft. Exhibit No. 32. Filed 8/17, 1942. Edmund L. Smith, Clerk. By J. M. Horn, Deputy Clerk. [45]

EXHIBIT 5-a

Petent and Copyright Office
Communication Should Be Addressed
"The Commissioner of Patents"
"Ottawa"

When Writing on This Subject Refer to
Serial Number of Application

Patent Office

Canada

Ottawa, June 23, 1942.

NOTICE OF ALLOWANCE

APPLICATION FOR PATENT

Serial No. 482127,
Inventor J. C. Ballagh,
Invention Protector for Drill Pipe,

I beg to inform you that the above application for patent has been examined and allowed.

The final fee, Twenty Dollars, must be paid not later than six months from the date of this notice of allowance.

The serial number of application, full name of inventor, title of invention, and date of allowance Must be given when paying final fee.

The preparation of the patent for signing and sealing will require about six weeks, and such work will not be undertaken until after the payment of the final fee. The Office delivers a Patent upon the day of its date.

The Patent will be published in the Canadian Patent Office Record of the date of the issue of the Patent.

Your obedient servant,

J. T. MITCHELL
Commissioner

To Messrs. Smart & Biggar, Victoria Bldg., Ottawa, Ont.

Circular 12. 20,000-6-3-41.

[Endorsed]: Deft. Exhibit No. 33. Filed 8/17, 1942. Edmund L. Smith, Clerk. By J. M. Horn, Deputy Clerk. [46]

EXHIBIT 5-b

Patent and Copyright Office
Communications Should Be Addressed
"The Commissioner of Patents"
"Ottawa"
When Writing on This Subject Refer to
Serial Number of Application

Patent Office
Canada
Ottawa, June 23, 1942.

NOTICE OF ALLOWANCE

APPLICATION FOR PATENT

Serial No. 482128,
Inventor De M. G. Miller,
Invention Open Hole Tool Joint Protector,

I beg to inform you that the above application for patent has been examined and allowed.

The final fee, Twenty Dollars, must be paid not later than six months from the date of this notice of allowance.

The serial number of application, full name of inventor, title of invention, and date of allowance Must be given when paying final fee.

The preparation of the patent for signing and sealing will require about six weeks, and such work will not be undertaken until after the payment of the final fee. The Office delivers a Patent upon the day of its date.

The Patent will be published in the Canadian Patent Office Record of the date of the issue of the Patent.

Your obedient servant,

J. T. MITCHELL
Commissioner

To Messrs. Smart & Biggar, Victoria Bldg., Ottawa, Ont.

Circular 12. 20,000-6-3-41.

[Endorsed]: Deft. Exhibit No. 34. Filed 8/17, 1942. Edmund L. Smith, Clerk. By J. M. Horn, Deputy Clerk. [47]

EXHIBIT 6

AFFIDAVIT OF JAMES E. BEDNAR

State of California,
County of Los Angeles—ss.

James E. Bednar, being first duly sworn, deposes and says: That he is associated with the firm of Musick and Burrell and Howard Burrell, the attorneys for the defendants, and each of them, herein, and that he participated in the trial of the above entitled case; that the trial of the above entitled case commenced on or about July 2, 1942, and continued until the afternoon of July 7, 1942.

In the trial of said case plaintiff introduced evidence to the effect that and contended that said devices referred to at the trial as the lip protector and the open hole tool joint protector were of doubtful patentability.

Affiant is informed and believes, and therefore states that on July 8, 1942, after the trial and submission of the above entitled cause, defendants received notice from their patent attorneys, Lyon & Lyon, which firm is acting as associate counsel for plaintiff in the instant case, that the Canadian Patent Office had allowed a patent upon the application of defendant D. G. Miller in respect to the open hole tool joint protector, and a patent upon the application of defendant J. C. Ballagh in respect to the lip protector. [48]

That it appears by reason of the exhibits attached to this petition that defendant D. G. Miller, on April

16, 1941, filed an application with the Canadian Patent Office, Serial No. 482128 in respect to the open hole tool joint protector; that on April 10, 1941, said defendant assigned all patent rights that might be obtained upon said application to the defendant corporation, free of royalty; that on June 23, 1942, this application for patent was allowed and that on July 8, 1942, defendants received notice of the same for the first time.

That it appears by reason of the exhibits attached to this petition that defendant J. C. Ballagh, on April 16, 1941, filed an application with the Canadian Patent Office, Serial No. 482127 in respect to the lip protector; that on April 10, 1941, said defendant assigned all patent rights that might be obtained upon said application to the defendant corporation, free of royalty; that on June 23, 1942, said application for patent in respect to the lip protector was allowed by the Canadian Patent Office, and that on July 8, 1942, defendants, and each of them, received notice of the same for the first time.

That affiant has been handling the trial of the above entitled case on behalf of the defendants and was necessarily absent from the City of Los Angeles from July 7, 1942, until July 26, 1942, for the purpose of trying another case in Tulsa, Oklahoma; that the foregoing newly discovered evidence was not brought to affiant's attention until his return to his office on July 27.

That this motion is not being made for any purpose of delay, but for the purpose of indicating to

the Court that the devices in question are definitely patentable.

JAMES E. BEDNAR

Subscribed and Sworn To before me this 31st day of July, 1942.

[Seal] ESSIE McCORMICK,
Notary Public in and for the County of Los Angeles, State of California.

[Endorsed]: Filed Aug. 4, 1942. Edmund L. Smith, Clerk. By P. D. Hooser, Deputy Clerk. [49]

At a stated term, to wit: The February Term, A. D. 1942 of the District Court of the United States of America, within and for the Central Division of the Southern District of California, held at the Court Room thereof, in the City of Los Angeles on Monday the 17th day of August in the year of our Lord one thousand nine hundred and forty-two.

Present:

The Honorable: Dave W. Ling, District Judge.

[Title of Cause.]

No. 1762-Y Civil

ORDER THAT MOTION TO RE-OPEN CASE STAND SUBMITTED

This cause coming on for hearing on motion of defendants to re-open the case to admit newly dis-

covered evidence, pursuant to notice filed August 4, 1942; Donald Y. Lamont, Esq., appearing as counsel for the plaintiff; J. E. Bednar, Esq., appearing as counsel for the defendants; and H. A. Dewing, Court Reporter, being present and reporting the proceedings:

Attorney Lamont makes an objection to motion to re-open. Attorney Bednar makes a statement and offers the following exhibits in behalf of the defendants and it is ordered that the said exhibits be admitted in evidence, to wit:

Defts' Ex. 28—Copy of letter, dated 5/12/41, from Lyon & Lyon to Patterson-Ballagh Corp.

Defts' Ex. 29—Assignment by James Courtenay Ballagh to Patterson-Ballagh Corp. together with affidavit of Howard Coleman Armington.

Defts' Ex. 30—Assignment by DeMont George Miller to Patterson-Ballagh Corp. together with affidavit of Howard Coleman Armington.

Defts' Ex. 31—Copy of letter, dated 7/7/42, from Lyon & Lyon to Patterson-Ballagh Corp.

Defts' Ex. 32—Copy of Letter, dated 7/7/42, from Lyon & Lyon to Patterson-Ballagh Corp. [50]

Defts' Ex. 33—"Notice of Allowance", from J. T. Mitchell, Commissioner, Patent Office, Ottawa, Canada, to Messrs. Smart & Biggar, Victoria Bldg., Ottawa, Ont.

Defts' Ex. 34—"Notice of Allowance" from J. T. Mitchell, Commissioner, Patent Office, Ottawa, Ontario, Canada, to Messrs. Smart & Biggar, Victoria Bldg., Ottawa, Ont.

It is ordered that the said motion to re-open stand submitted.
28/942 [51]

At a stated term, to wit: The February Term, A. D. 1942 of the District Court of the United States of America, within and for the Central Division of the Southern District of California, held at the Court Room thereof, in the City of Los Angeles on Monday the 31st day of August in the year of our Lord one thousand nine hundred and forty-two.

Present:

The Honorable: Dave W. Ling, District Judge.

[Title of Cause.]

No. 1762-Y Civil

ORDER FINDING IN FAVOR OF DEFENDANTS

This cause having been heretofore heard by the Court, on evidence both oral and documentary, and counsel having argued the cause, and the Court having duly considered the same and being fully advised,

The Court now finds in favor of the defendants, and it is ordered that Findings of Fact, Conclusions of Law, and Judgment be entered accordingly, counsel to prepare and present formal Findings and Judgment pursuant to local Rule 8.
29/110 [52]

[Title of District Court and Cause.]

FINDINGS OF FACT AND CONCLUSIONS OF LAW

The above entitled cause came on regularly for trial on July 1, 1942, at 10:00 o'clock A.M. in Courtroom No. 4 of the above entitled Court, Honorable Dave W. Ling, presiding, without a jury; motion of defendants, and each of them, to file an amendment to their answer was duly and regularly granted on July 1, 1942, and the case continued until July 2, 1942; thereafter the cause was tried on the 2nd, 3rd, 6th and 7th days of July, 1942, plaintiff Byron Jackson Co., a corporation, being represented by its attorneys, Chickering & Gregory and Lyon & Lyon, by Donald Y. Lamont, and defendants Patterson-Ballagh Corporation, a corporation, J. C. Ballagh and D. G. Miller being represented [53] by their attorneys, Musick and Burrell, by James E. Bednar; after argument by counsel, said cause was submitted to the Court for its decision on July 7, 1942; thereafter, without opposition and pursuant to motion of said defendants, and each of them, said cause was duly and regularly reopened August 17, 1942, to admit certain newly discovered evidence on behalf of said defendants, and each of them, and was thereupon resubmitted to the Court for its decision on August 17, 1942; evidence, both oral and documentary, having been introduced and presented, and the cause having

been argued by counsel and submitted to the Court for its decision as aforesaid, the Court now makes its Findings of Fact and Conclusions of Law as follows:

FINDINGS OF FACT

I.

It is true that plaintiff, Byron Jackson Co., is now, and at all times mentioned herein has been, a corporation organized and existing under and by virtue of the laws of the State of Delaware; that defendant Patterson-Ballagh Corporation is now, and at all times mentioned herein has been, a corporation organized and existing under and by virtue of the laws of the State of California, with its principal place of business in the County of Los Angeles, State of California, in the Southern District of California, Central Division; that defendant J. C. Ballagh is now, and at all times mentioned herein has been, a citizen and resident of the County of Los Angeles, State of California; and that defendant D. G. Miller is now, and since October, 1938, has been, a citizen and resident of the County of Los Angeles, State of California. [54]

II.

It is true that the jurisdiction of this Court is based upon diversity of citizenship; that this is a suit of a civil nature between citizens of different states; and that the amount in controversy exceeds, exclusive of interest and costs, the sum of $3,000.

III.

It is true that defendant Patterson-Ballagh Corporation now has, and at all times subsequent to September 20, 1928, has had, exactly 1,000 shares of its capital stock issued and outstanding; that defendant J. C. Ballagh is now, and continuously since September 20, 1928, has been, the record and beneficial owner of 125 shares of defendant Patterson-Ballagh Corporation; that defendant J. C. Ballagh and his wife are now, and continuously since on or about August 8, 1931, have been, the beneficial owners of 250 shares of defendant Patterson-Ballagh Corporation, which said 250 shares now stand, and at all times since on or about August 8, 1931, have stood, in the name of Highland Investment Corporation, Ltd., a corporation, as the record owner thereof; that said Highland Investment Corporation, Ltd., a corporation, is now, and at all times since on or about August 8, 1931, has been owned entirely by defendant J. C. Ballagh and his wife; that defendant D. G. Miller is now, and continuously since on or about February 15, 1939, has been, the beneficial owner of 375 shares of defendant Patterson-Ballagh Corporation, which said 375 shares now stand, and continuously since prior to February 15, 1939, have stood, in the name of one C. L. Patterson, as the record owner thereof; that defendant D. G. Miller purchased said 375 shares from said C. L. Patterson on or about February 15, 1939; that plaintiff is now, and continuously since September 20, 1928, has been the [55] beneficial owner of 250 shares of defendant

Patterson-Ballagh Corporation, and all of said 250 shares now stand, and during said period of time have stood, in the name of plaintiff as the record owner thereof, except for one share which now stands, and during said period of time has stood, in the name of a representative and nominee of plaintiff.

IV.

It is true that, at the present time, and at all times since February 15, 1939, the board of directors of defendant Patterson-Ballagh Corporation has consisted of five persons; that from February 15, 1939, to June 27, 1939, said board of directors was composed of H. C. Armington, H. W. Elliott, E. S. Dulin, defendant J. C. Ballagh, and defendant D. G. Miller; that said board is now, and continuously since June 27, 1939, has been, composed of H. C. Armington, E. S. Dulin, Howard Burrell, defendant J. C. Ballagh and defendant D. G. Miller; that said E. S. Dulin is now, and continuously since prior to October 1, 1936, has been, a member of the said board of directors of defendant Patterson-Ballagh Corporation; that said E. S. Dulin is now, and continuously since prior to October 1, 1936, has been the president of plaintiff and plaintiff's representative upon the said board of directors of defendant Patterson-Ballagh Corporation.

It is further true that defendant D. G. Miller is now, and at all times since February 15, 1939, has been, president of defendant Patterson-Ballagh Corporation, and that defendant J. C. Ballagh is now, and at all times since prior to September 20, 1928,

has been, the secretary-treasurer of defendant Patterson-Ballagh Corporation.

Each and every allegation set forth in paragraph IV of plaintiff's complaint herein is untrue, except for those allegations [56] which are specifically found to be true in these findings.

V.

It is true that since February 15, 1939, defendant J. C. Ballagh, as secretary-treasurer, and defendant D. G. Miller, as president, have, pursuant to and subject to the instructions, advice, supervision and direction of the board of directors of defendant Patterson-Ballagh Corporation, directed the affairs of said corporation and carried on its business, and that at all times said individual defendants have discharged their duties as such officers faithfully, efficiently, conscientiously, loyally and meritoriously.

Each and every allegation set forth in paragraph V of plaintiff's complaint herein is untrue, except for those allegations which are specifically found to be true in these findings.

VI.

It is true that, pursuant to and in accordance with resolutions duly, regularly and legally adopted by the board of directors of defendant Patterson-Ballagh Corporation, but over the protest of said E. S. Dulin, plaintiff's representative upon said board, defendant Patterson-Ballagh Corporation paid to defendant J. C. Ballagh the following com-

pensation for services rendered by said defendant J. C. Ballagh to defendant Patterson-Ballagh Corporation: the total sum of $15,000 during the calendar year 1939, the total sum of $30,166.66 during the calendar year 1940, and the total sum of $19,000 from January 1, 1941, to the time when plaintiff filed this action herein on September 10, 1941.

It is further true that the services rendered by defendant J. C. Ballagh to defendant Patterson-Ballagh Corporation from January 1, 1939, to the time of filing suit herein on September 10, 1941, were, are now and will continue to be of very [57] great value to said corporation, and that said services were performed loyally, efficiently, carefully and effectively.

It is further true that said compensation so paid to defendant J. C. Ballagh during the aforementioned periods of time was fair, just and reasonable as to the defendant Patterson-Ballagh Corporation at the various times it was authorized, approved and paid; and that defendant J. C. Ballagh did not at any time, as a member of the board of directors, vote upon any resolution concerning his own compensation. It is further true that every resolution of the board of directors concerning the aforementioned compensation of defendant J. C. Ballagh was adopted at meetings of said board when there was a legal quorum of said board present and that every such resolution was approved in good faith by an independent and disinterested majority of the directors present at such meetings.

It is further true that the compensation so paid

to defendant J. C. Ballagh during the calendar year 1939 was approved and ratified by a resolution duly, regularly and legally adopted by the beneficial and record owners of a majority of the issued and outstanding shares of Patterson-Ballagh Corporation at an annual meeting of said shareholders on January 16, 1940; that the compensation so paid to defendant J. C. Ballagh during the calendar year 1940 was approved and ratified by a resolution duly, regularly and legally adopted by the beneficial and record owners of a majority of the issued and outstanding shares of Patterson-Ballagh Corporation at an annual meeting of said shareholders on January 21, 1941; that the compensation so paid to defendant J. C. Ballagh from January 1, 1941, to the time when plaintiff filed suit herein on September 10, 1941, was approved and ratified by a resolution duly, regularly and legally adopted by the beneficial and record [58] owners of a majority of the issued and outstanding shares of Patterson-Ballagh Corporation at an annual meeting of said shareholders on January 20, 1942; and that the aforementioned three resolutions of shareholders approving the compensation so paid to defendant J. C. Ballagh as aforesaid were adopted in good faith, and without fraud, actual or constructive, by each and all of the shareholders voting for them.

Each and every allegation set forth in paragraph VI of plaintiff's complaint herein is untrue, except for those allegations which are specifically found to be true in these findings.

VII.

It is true that, pursuant to and in accordance with resolutions duly, regularly and legally adopted by the board of directors of defendant Patterson-Ballagh Corporation, said corporation paid to defendant D. G. Miller the following compensation for services rendered by said defendant D. G. Miller to defendant Patterson-Ballagh Corporation: the total sum of $19,750 during the calendar year 1940, and the total sum of $12,000 from January 1, 1941, to and including September 10, 1941, at which time plaintiff commenced its action herein. It is further true that, beginning in December, 1940, said E. S. Dulin, plaintiff's representative upon said board, objected to the compensation paid to defendant D. G. Miller as aforesaid.

It is further true that the services rendered by defendant D. G. Miller to defendant Patterson-Ballagh Corporation from January 1, 1940, to the time of filing suit herein on September 10, 1941, were, are now, and will continue to be of very substantial value to said corporation, and that said services were performed loyally, efficiently, carefully and effectively.

It is further true that said compensation so paid to [59] defendant D. G. Miller during the aforementioned periods of time was fair, just and reasonable as to the defendant Patterson-Ballagh Corporation at the various times it was authorized, approved and paid; and that defendant D. G. Miller did not at any time, as a member of the board of directors, vote upon any resolution concerning his

own compensation. It is further true that every resolution of the board of directors concerning the aforementioned compensation of defendant D. G. Miller was adopted at meetings of said board when there was a legal quorum of said board present and that every such resolution was approved in good faith by an independent and disinterested majority of the directors present at such meetings.

It is further true that the compensation so paid to defendant D. G. Miller during the calendar year 1940 was approved and ratified by a resolution duly, regularly and legally adopted by the beneficial and record owners of a majority of the issued and outstanding shares of Patterson-Ballagh Corporation at an annual meeting of said shareholders on January 21, 1941; that the compensation so paid to defendant D. G. Miller from January 1, 1941, to the time when plaintiff filed suit herein on September 10, 1941, was approved and ratified by a resolution duly, regularly and legally adopted by the beneficial and record owners of a majority of the issued and outstanding shares of Patterson-Ballagh Corporation at an annual meeting of said shareholders on January 20, 1942; and that the aforementioned two resolutions of shareholders approving the compensation so paid to defendant D. G. Miller as aforesaid were adopted in good faith, and without fraud, actual or constructive, by each and all of the shareholders voting for them.

Each and every allegation set forth in paragraph VII of [60] plaintiff's complaint herein is untrue,

except for those allegations which are specifically found to be true in these findings.

VIII.

It is true that defendant Patterson-Ballagh Corporation has not declared or paid any dividends to its shareholders since July, 1938.

Each and every allegation set forth in paragraphs VIII and IX of plaintiff's complaint herein is untrue, except for those allegations which are specifically found to be true in these findings.

IX.

It is true that plaintiff is now, and has been since September 20, 1928, a stockholder of defendant Patterson-Ballagh Corporation and that this action is not a collusive one to confer on a court of the United States jurisdiction of any action of which it would not otherwise have jurisdiction.

X.

It is true that, prior to the bringing of this action, plaintiff attempted to secure from the directors and stockholders of Patterson-Ballagh Corporation action by said corporation in the bringing and prosecution of this suit by taking the following steps: on or about August 5, 1941, plaintiff served upon the board of directors of defendant Patterson-Ballagh Corporation a demand in words and figures as set forth in Exhibit A attached to plaintiff's complaint herein; on or about August 8, 1941, plaintiff caused E. S. Dulin, who is, and at all times mentioned herein was, plaintiff's presi-

dent and the representative of plaintiff upon the board of directors of Patterson-Ballagh Corporation, to deliver to defendant D. G. Miller as president of said defendant corporation, a letter in words and figures as set forth in Exhibit B attached to [61] plaintiff's complaint herein; on or about August 14, 1941, plaintiff delivered to each stockholder of said defendant corporation, except plaintiff, a letter in words and figures as set forth in Exhibit C attached to plaintiff's complaint herein.

XI.

It is true that, prior to the filing of this suit, neither the directors nor the stockholders of defendant Patterson-Ballagh Corporation took any action in response to the demands of plaintiff as set forth in paragraph X of these findings.

Each and every allegation set forth in paragraph XII of plaintiff's complaint herein is untrue, except for those allegations which are specifically found to be true in these findings.

XII.

It is true that at all times mentioned in the complaint, E. S. Dulin was the duly appointed and acting agent of plaintiff, and was acting within the scope of his authority as such agent, in respect to the affairs of defendant Patterson-Ballagh Corporation; that on January 21, 1941, an annual meeting of shareholders of defendant Patterson-Ballagh Corporation was duly and regularly held at which there were present in person or by proxy all shareholders of said defendant corporation, in-

cluding said E. S. Dulin, who at that time represented the 250 issued and outstanding shares beneficially owned by plaintiff; that at said annual meeting, H. C. Armington, Howard Burrell, E. S. Dulin, defendant J. C. Ballagh and defendant D. G. Miller were nominated to serve as directors during the ensuing year, or until election or appointment of their successors; that after said nominations, it was moved by defendant J. C. Ballagh, seconded by said E. S. Dulin, and unanimously resolved that said nominations be closed and that the secretary of the corporation be instructed to cast a unanimous [62] ballot on behalf of all shareholders present in favor of the persons nominated as directors as aforesaid; that said secretary thereupon cast said ballot and said nominees were duly elected directors for the ensuing year; that on January 21, 1941, and following the meeting of shareholders hereinbefore referred to, a meeting of the board of directors of defendant Patterson-Ballagh Corporation was duly and regularly held, at which all directors, including said E. S. Dulin, were present; that at said board meeting, defendant D. G. Miller was nominated for president, defendant J. C. Ballagh was nominated for secretary and treasurer, and one M. G. Nolan was nominated for assistant secretary and assistant treasurer; that after said nominations, and on motion duly seconded and unanimously carried by the vote of all persons present, including said E. S. Dulin, it was resolved that all nominations

be closed and that the persons nominated as officers as aforesaid for the ensuing year be elected and appionted as such by acclamation; that prior to the election of said directors as aforesaid, and prior to the election of said officers as aforesaid, said E. S. Dulin, representing plaintiff, had no notice or knowledge that the attitude of said H. C. Armington, Howard Burrell, J. C. Ballagh, and D. G. Miller in respect to the matters of compensation complained of in the complaint would be any different for the ensuing year of 1941 from what said persons' attitude had been toward said compensation matters during 1940 when said H. C. Armington, Howard Burrell, J. C. Ballagh, and D. G. Miller likewise constituted four of the five directors on the board of Patterson-Ballagh Corporation; that, prior to participating in and approving the election of said persons as directors and officers on January 21, 1941, as aforesaid, said E. S. Dulin, representing plaintiff, knew the attitude of said persons concerning the compensation that [63] said persons considered should properly be paid to defendant J. C. Ballagh and defendant D. G. Miller during 1941; that plaintiff has waived any right that it might have to complain of the compensation paid to defendants J. C. Ballagh and D. G. Miller by defendant Patterson-Ballagh Corporation from January 1, 1941, to the time of filing suit herein on September 10, 1941.

CONCLUSIONS OF LAW

I.

That the compensation paid by defendant Pat-

terson-Ballagh Corporation to defendant J. C. Ballagh from January 1, 1939, to the time of filing suit herein on September 10, 1941, has been fair, just and reasonable as to said corporation at the various times that it was authorized, approved and paid.

II.

That the compensation paid by defendant Patterson-Ballagh Corporation to defendant D. G. Miller from January 1, 1940, to the time of filing suit herein on September 10, 1941, has been fair, just and reasonable as to said corporation at the various times that it was authorized, approved and paid.

III.

That plaintiff has waived any right to complain of the compensation paid by defendant Patterson-Ballagh Corporation to defendants J. C. Ballagh and D. G. Miller from January 1, 1941, to the time of filing suit herein on September 10, 1941.

IV.

That plaintiff is not entitled, either on its own behalf, or on behalf of Patterson-Ballagh Corporation, or otherwise, to any relief or recovery whatsoever against any of the defendants herein.

[64]

V.

That each of the defendants herein is entitled to recover of and from plaintiff his or its respective costs of suit incurred herein.

Judgment is ordered to be entered accordingly.

Dated this 29 day of September, 1942.

DAVE W LING
Judge of the United States
District Court

Approved as to form this __ day of _____, 1942.

CHICKERING & GREGORY
DONALD Y. LAMONT
LYON & LYON
LEONARD S. LYON
IRWIN L. FULLER
Attorneys for Plaintiff

Received copy of the within Findings of Fact and Conclusions of Law this __ day of September, 1942.

CHICKERING & GREGORY
DONALD Y. LAMONT
LYON & LYON
LEONARD S. LYON
IRWIN L. FULLER
Attorneys for Plaintiff

[Endorsed]: Filed Sep. 30, 1942. [65]

In the District Court of the United States
Southern District of California
Central Division

Civil Action No. 1762-Y

BYRON JACKSON CO., a corporation,
Plaintiff,

vs.

PATTERSON-BALLAGH CORPORATION, a corporation, J. C. BALLAGH and D. G. MILLER,
Defendants.

FINAL JUDGMENT

The above entitled cause came on regularly for trial on July 1, 1942, in Courtroom No. 4 of the above entitled Court, Honorable Dave W. Ling, Judge, presiding, without a jury, and was thereafter tried on July 2, 3, 6, 7 and August 17, 1942, plaintiff Byron Jackson Co., a corporation, being represented by its attorneys Chickering & Gregory and Lyon & Lyon, by Donald Y. Lamont, and defendants Patterson-Ballagh Corporation, a corporation, J. C. Ballagh and D. G. Miller being represented by their attorneys Musick and Burrell, by James E. Bednar; evidence, both oral and documentary, having been introduced, and the cause having been argued by counsel and submitted to the [66] Court for its decision, and the Court having made its written Findings of Fact and Conclusions of Law, and being fully advised in the premises,

It Is Hereby Ordered, Adjudged and Decreed that plaintiff take nothing by its action herein, either on its own behalf, or on behalf of defendant Patterson-Ballagh Corporation, or otherwise, and that defendants Patterson-Ballagh Corporation, a corporation, J. C. Ballagh and D. G. Miller do have and recover from plaintiff Byron Jackson Co., their costs and disbursements incurred herein and taxed in the sum of $ _____

Dated this 29 day of Sept., 1942.

DAVE W. LING
Judge of the United States
District Court

Approved as to form this __ day of _____, 1942.

CHICKERING & GREGORY
DONALD Y. LAMONT
LYON & LYON
LEONARD S. LYON
IRWIN L. FULLER
Attorneys for Plaintiff

Received full and entire satisfaction on the within costs this 10th day of October 1942.

Witness: Edmund L. Smith, Clerk. By Theodore Hocke Deputy.

MUSICK & BURRELL
HOWARD BURRELL
Attorneys for Defendants

Judgment entered Sep. 30—1942 Docketed Sep. 30—1942 C. O. Book 11 Page 514 Edmund L. Smith, Clerk, By J. M. Horn, Deputy

Received copy of the within Final Judgment this -- day of ------, 1942.

CHICKERING & GREGORY
DONALD Y. LAMONT
LYON & LYON
LEONARD S. LYON
IRWIN L. FULLER
Attorneys for Plaintiff

[Endorsed]: Filed Sep. 30, 1942 [67]

[Title of District Court and Cause.]

MOTION FOR NEW TRIAL

To the Above Entitled Court and the Clerk Thereof, and to the Above Named Defendants and Their Attorneys:

Plaintiff above named moves the above entitled Court for an order vacating and setting aside the findings of fact and conclusions of law and the judgment entered thereon upon September 30, 1942, and granting a new trial in the above entitled action, upon the following grounds:

(1) Errors in law occurring at the trial and excepted to by the plaintiff.

(2) Insufficiency of the evidence to justify the findings of fact and conclusions of law.

(3) Insufficiency of the evidence to justify the judgment. [68]

(4) The said findings of fact and conclusions of law are against law.

(5) The said judgment is against law.

Dated, October ------, 1942.

CHICKERING & GREGORY
DONALD Y. LAMONT
LYON & LYON
LEONARD S. LYON
IRWIN L. FULLER
Attorneys for Plaintiff.

[Endorsed]: Filed Oct 9, 1942. [69]

[Title of District Court and Cause.]

NOTICE OF MOTION OF PLAINTIFF FOR A NEW TRIAL AND FOR A HEARING THEREOF

To the Above Entitled Court and the Clerk Thereof, and to the Above Named Defendants and Their Attorneys:

Notice Is Hereby Given You, and Each of You, that plaintiff in the above entitled action has filed, or is about to file, a motion to vacate and set aside the findings of fact and conclusions of law of the Court made herein, and the judgment entered thereon on September 30, 1942, and for a new trial in the above entitled action, upon the grounds set forth in said motion, copy of which motion is herewith served upon you.

Notice Is Further Hereby Given You, and Each of You, that on Monday, the 19th day of October,

1942, in the Court Room of the above entitled Court in the Federal Building, Los Angeles, [70] California, at 10:00 o'clock in the forenoon of said day, or as soon thereafter as the same may be heard, plaintiff will bring on said motion for hearing.

You Are Hereby Further Notified that said motion is based upon the minutes of the Court and all of the records and files in the above entitled action.

Dated, October 9th, 1942.

CHICKERING & GREGORY
DONALD Y. LAMONT
LYON & LYON
LEONARD S. LYON
IRWIN L. FULLER
Attorneys for Plaintiff.

[Endorsed]: Filed Oct 9, 1942 [71]

[Title of District Court and Cause.]

STIPULATION CONCERNING DISPOSITION OF MOTION FOR NEW TRIAL

It Is Hereby Stipulated by and between the parties to the above entitled action, through their attorneys of record, that plaintiff's pending motion for new trial shall be heard and determined by Judge Dave W. Ling sitting at Phoenix, Arizona, upon briefs to be submitted by the parties as hereinafter set forth, without oral argument, and that

the decision and any order upon said motion made by said Judge Ling at Phoenix, Arizona, when transferred to and filed in the above entitled Court, shall have the same force and effect as if made by said Judge Ling within this District.

It is further stipulated that plaintiff will serve and file with the clerk of the above entitled court its opening brief [72] within ten days from the receipt by plaintiff's counsel of the exhibits sent by counsel for defendants to counsel for plaintiff at San Francisco; that counsel for defendants will serve and file with the Clerk of the above entitled court their answering brief within ten days after plaintiff's opening brief has been served and filed; that plaintiff may have five days from and after the receipt of defendants' answering brief in which to serve and file with the clerk of the above entitled court a reply thereto.

It is further stipulated that the clerk of the above entitled court shall forward to Judge Dave W. Ling the pleadings in the above entitled case, including plaintiff's motion for new trial and the respective briefs of the parties, to be filed as hereinbefore set forth, together with such exhibits and such parts of the Reporter's Transcript as Judge Dave W. Ling may desire; and that upon the serving and filing of the briefs as aforesaid the cause may stand submitted.

Dated this 2nd day of Nov, 1942.

CHICKERING & GREGORY
DONALD Y. LAMONT
LYON & LYON
LEONARD S. LYON
IRWIN L. FULLER
By IRWIN L. FULLER
Attorneys for Plaintiff

MUSICK AND BURRELL and
HOWARD BURRELL
By HOWARD BURRELL
Attorneys for Defendants

Approved and So Ordered this 2nd day of November, 1942. Mr. Fuller having stated that arrangement of stipulation is satisfactory to Judge Ling.

PAUL J. McCORMICK
Judge

[Endorsed]: Filed Nov. 2, 1942 [73]

At a stated term, to wit: The September Term, A. D. 1942 of the District Court of the United States of America, within and for the Central Division of the Southern District of California, held at the Court Room thereof, in the City of Los Angeles on Monday the 30th day of November in the year of our Lord one thousand nine hundred and forty-two.

Present:

The Honorable: Leon R. Yankwich, District Judge

[Title of Cause.]

No. 1762-Y Civil

This cause coming on for hearing on motion for a new trial; I. L. Fuller, Esq., of Lyon & Lyon, appearing as counsel for Plaintiff, states that motion is under submission to Judge Ling on briefs by stipulation.

30/785 [74]

At a stated term, to wit: The February Term, A. D. 1943 of the District Court of the United States of America, within and for the Central Division of the Southern District of California, held at the Court Room thereof, in the City of Los Angeles on Monday the 22nd day of February in the year of our Lord one thousand nine hundred and forty-three.

Present:

The Honorable: Dave W. Ling, District Judge

[Title of Cause.]

No. 1762-Y Civil

ORDER DENYING MOTION FOR NEW TRIAL

This cause came on for hearing on the motion of plaintiff for a new trial. Upon consideration

whereof, it is now here ordered that said motion be, and the same hereby is denied.

Dated: Phoenix, Arizona, February 19, 1943.

DAVE W. LING
Judge

32/184

[Endorsed]: Filed Feb 22, 1943 [75]

Dave W. Ling
District Judge
United States District Court
District of Arizona

Judge's Chambers
Phoenix, Arizona
March 9th, 1943.

Clerk, U. S. District Court,
Federal Building,
Los Angeles, Calif.

Re: Byron Jackson Co. v Patterson-Ballagh Corporation, #1762-Y Civil

Dear Sir:

Counsel in the above matter have directed my attention to an error appearing in the order denying plaintiff's motion for a new trial filed February 22d.

The order recites "This cause came on for hearing on the motion of defendant for a new trial". It should be corrected to read "on the motion of

plaintiff''. This is your authorization to make such correction by interlineation.

Very truly yours,
DAVE W LING

cc—Musick, Burrell & Pinney
Chickering & Gregory
DWL/b. [76]

[Title of District Court and Cause.]

NOTICE OF ENTRY OF ORDER DENYING NEW TRIAL

To the Plaintiff Above Named and to Messrs. Chickering & Gregory and Donald Y. Lamont, Esq., 111 Sutter Street, San Francisco, California, and Lyon & Lyon, Leonard S. Lyon, Esq., and Irwin L. Fuller, Esq., 811 West Seventh Street, Los Angeles, California, Its Attorneys:

You, and Each of You, Will Please Take Notice that the District Court of the United States, for the Southern District of California, Central Division, entered its order herein on the 19th day of February, 1943, denying the motion of plaintiff for a new trial in the cause above entitled.

Dated this 16th day of March, 1943.

MUSICK AND BURRELL and
HOWARD BURRELL
By ANSON B. JACKSON JR.
Attorneys for Defendants

[Endorsed]: Filed Mar. 17, 1943 [77]

[Title of District Court and Cause.]

NOTICE OF APPEAL TO THE CIRCUIT COURT OF APPEALS FOR THE NINTH CIRCUIT UNDER RULE 73(b) OF THE RULES OF CIVIL PROCEDURE FOR THE DISTRICT COURTS OF THE UNITED STATES

To Defendants Patterson-Ballagh Corporation, a corporation, J. C. Ballagh and D. G. Miller, and to Musick and Burrell and Howard Burrell, their attorneys:

Notice Is Hereby Given that Byron Jackson Co., a corporation, plaintiff above named, hereby appeals to the Circuit Court of Appeals for the Ninth Circuit from the final judgment entered in this action on September 30, 1942.

Dated, May 11, 1943.

DONALD Y. LAMONT
FREDERICK M. FISK
CHICKERING & GREGORY
111 Sutter Street,
San Francisco, California, [78]
LYON & LYON
LEONARD S. LYON
IRWIN L. FULLER
811 West Seventh Street,
Los Angeles, California,
Attorneys for Plaintiff.

[Endorsed]: Filed & Mailed Copy to Musick & Burrell, Attys. for Defts. May 15, 1943. [79]

[Title of District Court and Cause.]

COST BOND

Know All Men by These Presents, That:

Byron Jackson Co., a corporation, duly organized under the laws of the State of Delaware and having an office and principal place of business in Vernon, Los Angeles County, California, as principal, and Pacific Indemnity Company, a corporation duly organized under the laws of the State of California and having an office and principal place of business at Los Angeles, California, as surety, are held and firmly bound unto Patterson-Ballagh Corporation, a corporation, J. C. Ballagh and D. G. Miller, in the full and just sum of Two Hundred Fifty Dollars ($250.00) to be paid to the said Patterson-Ballagh Corporation, a corporation, [80] J. C. Ballagh and D. G. Miller, their heirs, executors, administrators, successors or assigns, which payment well and truly to be paid the undersigned bind themselves by these presents.

Sealed with the seals of the undersigned and dated this 12 day of May, 1943, in the Year of our Lord One Thousand Nine Hundred and Forty-Three; and

Whereas, lately at a District Court of the United States for the Southern District of California, in a suit pending in said Court between Byron Jackson Co., a corporation, as plaintiff, and Patterson-Ballagh Corporation, a corporation, J. C. Ballagh and D. G. Miller, as defendants, a judgment was rendered against the said plaintiff and the said

plaintiff having filed in said Court a notice of appeal to reverse the said judgment in the aforesaid suit on appeal to the United States Circuit Court of Appeals for the Ninth Circuit, at a session of said Circuit Court of Appeals to be holden at Los Angeles in the State of California,

Now, the condition of the above obligation is such that if the said Byron Jackson Co. shall make payment of costs if the appeal be dismissed or the judgment affirmed, or of such costs as the Appellate Court may award if the judgment is modified, then the above obligation to be void, else to remain in full force and effect.

[Seal] BYRON JACKSON CO.,
a corporation,
By C. H. NAJRO
Vice President
And ----------
Secretary

Acknowledged before me this 12 day of May, 1943.

[Seal] MARIE O. BERRY
Notary Public in and for the County of Los Angeles, State of California
My Commission Expires March 15, 1947 [81]

[Seal] PACIFIC INDEMNITY COMPANY, a California corporation,
By C. A. SHAVER, JR
Its Attorney in Fact
By ----------
Its Attorney in Fact

State of California,
County of Los Angeles,—ss.

On this 12th day of May in the year one thousand nine hundred and 43 before me, Atala M. Carter a Notary Public in and for said County and State, residing therein, duly commissioned and sworn, personally appeared C. A. Shaver, Jr., known to me to be the duly authorized Attorney-in-Fact of Pacific Indemnity Company, and the same person whose name is subscribed to the within instrument as the Attorney-in-Fact of said Company, and the said C. A. Shaver, Jr. acknowledged to me that he subscribed the name of Pacific Indemnity Company, thereto as surety and his own name as Attorney-in-Fact.

In Witness Whereof, I have hereunto set my hand and affixed my official seal the day and year in this Certificate first above written.

[Seal] ATALA M. CARTER

Notary Public in and for Los Angeles County, State of California

My Commission Expires May 28, 1946

[Endorsed]: Filed May 15, 1943 [82]

DOCKET ENTRIES

Sept. 10, 1941—Fld compl for recovery of excess salaries & compensation Issd summons. Md JS-5

Oct. 1, 1941—Fld. stip. & ord. defts. have to & incl. 10/10/41 to plead compl.

Oct. 9, 1941—Fld. deft's not. of mo. to dismiss, retble. 10/27/41, 10 AM, & pts. auths. in suppt.

Oct. 14, 1941—Fld. plf's. pts. & auths.

Oct. 16, 1941—Fld. deft's reply. Memo of pts. & auths. in suppt. mo. to dismiss, etc.

Oct. 24, 1941—Fld. plf's additional pts. & auths.

Oct. 27, 1941—Ent. order denying defts mo to dismiss & allowing 20 days to answer

Nov. 17, 1941—Fld. stip. & ord. that defts. have to & incl. 11/29/41 to plead.

Nov. 28, 1941—Fld. Answer of deft's Patterson-Ballagh Corp., J. C. Ballagh & D. G. Miller to compl.

Feb. 12, 1942—Ent ord comtg to 4-6-42 for setting.

Mar. 25, 1942—Fld summons ret not served.

Apr. 6, 1942—Ent ord settg for trial 6/30/42.

June 26, 1942—Ent ord transf case to Cal of Jdg Ling & re-settg for trial.

June 29, 1942—Fld depos. of J. C. Ballagh & D. G. Miller. Fld depos of E. S. Dulin & 1 deft exs together with plfs exhs. 1 to 13 incl

July 1, 1942—Ent ord postponing hrg to 7-2-42.

July 2, 1942—Ent proc on hrg & ord contg to 7-3-42 fur hrg. Ser 2 plfs writs. Fld 18 plfs exs. Fld 6 defts exs. Fld amendment to answer.

July 3, 1942—Fld verification of compl. Ent proc on fur trial & ord contg fur trial to 7-6-42. Ser 3 plfs writs. Ser 2 writs for defts. Fld 1 plf ex. Fld 4 defts exs.

July 6, 1942—Ent proc on fur trial & ord contg to 7-7-42 fur trial. Ser 2 plfs writs. Fld 8 pfs exs. Fld 2 defts exs.

July 7, 1942—Ent proc on fur hrg & ent ord takg under submission before Jdg Dave W. Ling.

Aug. 4, 1942—Fld not of hearing of motion to reopen case to admit newly discovered evidence 8-10-42.

Aug. 17, 1942—Ent procs on hrg mo to reopen case to admit newly discovered evidence purs to not fld 8/4/42 & ent ord stand subm. Fld 7 defts exhs.

Aug. 31, 1942—Ent findg & ord for jdgmt favor defts; counsel to prepare & present formal findgs & judg accord. Not. counsel.

Sept. 1, 1942—Fld Reporter's Transc of final arguments of counsel.

Sept. 30, 1942—Fld findgs of fact & Concls of law & fld & ent in Co Bk 11/514 Final Jdgmt in favor of defts Patterson-Ballagh Corp., a corp. & J. C. Ballagh & D. G. Miller for costs incurred herein. D. & I. Same. Made Report JS-6.

Oct. 2, 1942—Fld not of entry of final jdgmt. Fld defts cost bill to be taxed 10 A.M. 10-5-42.

Oct. 5, 1942—Taxed costs of defts at $90.25. Dock & ent costs.

Oct. 9, 1942—Fld mot & not of mot of plf for new trial to be heard 10-19-42.

Oct. 10, 1942—Ent marginal satisf of costs. Dock same.

Oct. 14, 1942—Fld. ans. pts. & auths. in oppos. to plf's mot. for new trial.

Oct. 19, 1942—Ent ord contg 1 wk on mot for a new trial.

Oct. 26, 1942—Ent ord contg 5 wks (11/30/42) to hear mo for new trial to be heard by Judge Ling.

Nov. 2, 1942—Fld stip & ord thereon plfs mo for new trial be heard on briefs by Judge Ling sitting at Phoenix, Ariz.; plf to file openg brief whn 10 days receipt of exhs.; defts to file answg brief whn 10 days aft flg plfs brief; plf to have 5 days thereaft to file reply; further, clk to forward to J. Ling pleadings, etc.

Nov. 12, 1942—Fld plfs opening brief on mo for new trial. [83]

Nov. 16, 1942—Fld Reporter's Transcript of test & proc on trial.

Nov. 23, 1942—Fld stip & ord thereon extendg time defts to file answerg briefs to & inc 12-3-42, plf 5 days thereaft.

Nov. 30, 1942—Counsel state mo is under submission to Judge Ling on briefs fur stip.

Dec. 2, 1942—Fld answering brief defts on mo for new trial.

Dec. 4, 1942—Fld stip & ord thereon extending time plf to file reply brief to & inc 12-18-42.

Dec. 18, 1942—Fld plfs closing brief on mo for new trial.

Feb. 22, 1943—Fld & ent ord denying plfs. mo for a new trial.

Mar. 12, 1943—Recd letter from Judge Dave W. Ling amendg ord dated 2/22/43 chang word "deft" to "plf" in denyg mo for a new trial. Made correction by interlineation.

Mar. 17, 1943—Fld not of denial plfs mot for new trial.

May 15, 1943—Fld not plf of appeal CCA & mailed copy to Musick & Burrell attys for deft. Fld cost bond on appeal. Fld designation contents rel on appeal.

June 7, 1943—Fld stip re record on app. & ord re transmittal orig exhbs. to C.C.A. [84]

[Title of District Court and Cause.]

DESIGNATION OF CONTENTS OF RECORD ON APPEAL UNDER RULE 75 (a) OF THE RULES OF CIVIL PROCEDURE FOR THE DISTRICT COURTS OF THE UNITED STATES

Byron Jackson Co., a corporation, plaintiff above named, hereby designates as the record on appeal in the above entitled action and for inclusion and to be contained in such record the complete rec-

ord and all of the proceedings and all of the evidence in the action, and without limiting the generality thereof does hereby designate and specify that the following be included in said record:

(a) Certified copy of all entries concerning the above entitled action contained in the civil docket on file in the Clerk's office, commencing with September 10, 1941, the date of [85] the commencement of said action to the date hereof;

(b) Complaint, including all exhibits attached thereto;

(c) Stipulation and order granting defendants' time to plead to complaint, filed October 1, 1941;

(d) Defendants' notice of motion to dismiss, filed October 9, 1941;

(e) Minute order entered October 27, 1941, denying defendants' motion to dismiss, and allowing 20 days to answer;

(f) Stipulation and order granting defendants' time to plead, filed October 17, 1941;

(g) Answer of defendants to complaint, filed November 28, 1941;

(h) Minute order continuing case for setting, entered February 2, 1942;

(i) Summons filed March 25, 1942;

(j) Minute order setting case for trial, entered April 6, 1942;

(k) Minute order transferring case to calendar of Judge Ling, entered June 26, 1942;

(l) Depositions of J. C. Ballagh, D. G. Miller, and E. S. Dulin, together with all exhibits, filed June 29, 1942;

(m) Minute order postponing hearing, entered July 1, 1942;

(n) Proceedings on hearings and minute order continuing for further hearings, entered July 2, 1942, together with all plaintiff's and defendants' exhibits and defendants' amendment to answer, filed on said date;

(o) Verification of complaint, filed on July 3, 1942; also proceedings on trial and minute order concerning further trial, entered July 3, 1942; and also all plaintiff's and defendants' exhibits, filed July 3, 1942; [86]

(p) Proceedings on trial and minute orders concerning further trial, entered on July 6, 1942; also all plaintiff's and defendants' exhibits, filed on July 6, 1942;

(q) Proceedings concerning trial, entered July 7, 1942;

(r) Order taking cause under submission, entered July 7, 1942;

(s) Notice of motion to reopen the case to admit newly discovered evidence, filed August 4, 1942;

(t) Proceedings on hearing of motion to reopen, entered August 17, 1942; also amended order submitting motion to reopen case, entered on August 17, 1942; also all defendants' exhibits, filed on August 17, 1942;

(u) Findings and minute order for judgment in favor of defendants, entered August 31, 1942; also instructions to counsel regarding preparation of formal findings and judgment;

(v) Findings of Fact and Conclusions of Law, filed and entered on September 30, 1942;

(w) Final judgment, filed on September 30, 1942;

(x) Notice of entry of final judgment, filed October 2, 1942;

(y) Defendants' cost bill, filed on October 2, 1942;

(z) Order taxing costs, docketed and entered on October 5, 1942;

(aa) Motion, and notice of motion, for new trial, filed on October 9, 1942;

(bb) Marginal satisfaction of costs, entered and docketed October 10, 1942;

(cc) Minute order continuing hearing on motion for new trial, entered on October 19, 1942;

(dd) Minute order continuing hearing on motion for new trial, entered on October 26, 1942; [87]

(ee) Stipulation and order that motion for new trial be heard on briefs, filed and entered on November 2, 1942;

(ff) Reporter's transcript of testimony and proceedings on trial, filed on November 16, 1942;

(gg) Stipulation and order extending time to file answering briefs, filed and entered on November 23, 1942;

(hh) Stipulation regarding submission, entered in the docket on November 30, 1942;

(ii) Stipulation and order extending time to file reply brief, filed and entered on December 4, 1942;

(jj) Minute order denying motion for new trial, filed and entered on February 22, 1943;

(kk) Letter from Judge Dave W. Ling amending minute order dated February 22, 1943, received and entered on March 12, 1943;

(ll) Notice of denial of motion for new trial, filed on March 17, 1943;

(mm) Notice of appeal;

(nn) Cost bond on appeal;

(oo) The within designation of contents of record on appeal;

(pp) Certificate by Clerk of the United States District Court that the foregoing constitutes the complete and entire record, proceedings, and evidence in the said District Court.

Dated, May 14th, 1943.

CHICKERING & GREGORY
FREDERICK M. FISK
DONALD Y. LAMONT
111 Sutter Street
San Francisco, California

[88]

LYON & LYON
LEONARD S. LYON
IRWIN L. FULLER
811 West Seventh Street
Los Angeles, California.
Attorneys for Plaintiff.

[Endorsed]: Filed May 15, 1943. [89]

[Title of District Court and Cause.]

STIPULATION RE RECORD ON APPEAL AND ORDER RE TRANSMITTAL OF ORIGINAL PAPERS AND EXHIBITS

It Is Hereby Stipulated by and between the parties hereto as follows:

(I) The following items, heretofore included in plaintiff-appellant's designation of contents of record on appeal filed herein May 15, 1943, shall be omitted by the Clerk from the record on appeal in the above entitled action:

Items (c), (f), (h), (i), (j), (k), (l), (m), (x), (y), (z), (bb), (cc), (dd), (gg) and (ii).

(II) All original papers and exhibits and the depositions of J. C. Ballagh, D. G. Miller and E. S. Dulin together with all [90] exhibits thereto, shall be transmitted by the Clerk of this court to the Clerk of the Circuit Court of Appeals for the Ninth Circuit as a part of the record on appeal.

(III) The Court may, if it approves, enter the order annexed hereto for the transmittal by the Clerk of this Court of the original papers and exhibits in the above entitled cause and the depositions of J. C. Ballagh, D. G. Miller and E. S. Dulin to the Clerk of the Circuit Court of Appeals for the Ninth Circuit

(IV) This stipulation and the order annexed

hereto shall be included by the Clerk of this court in the said record on appeal.

Dated this 7th day of June, 1943.

DONALD Y. LAMONT
LEONARD S. LYON
IRWIN L. FULLER
Attorneys for Plaintiff-Appellant

MUSICK, BURRELL & PINNEY
ANSON B. JACKSON, Jr.
Attorneys for Defendants-Appellees

Approved and So Ordered this 7th day of June, 1943.

PAUL J. McCORMICK
Judge [91]

[Endorsed]: Filed Jun. 7, 1943.

[Title of District Court and Cause.]

ORDER RE TRANSMITTAL OF ORIGINAL PAPERS AND EXHIBITS AND DEPOSITIONS

It appearing that it is desirable that certain original papers and exhibits and depositions of J. C. Ballagh, D. G. Miller and E. S. Dulin together with all exhibits thereto, on file in the above entitled cause shall be sent to the Circuit Court of

Appeals for the Ninth Circuit in lieu of copies thereof, notice of appeal to that Court having been filed in this cause by plaintiff herein,

It Is Hereby Ordered, pursuant to Rule 75(i) of the Rules of Civil Procedure that the Clerk of this Court forward by express, all costs thereof to be paid by plaintiff-appellant, Byron Jackson Co., to the Clerk of the Circuit Court of Appeals for the Ninth Circuit, all original papers and exhibits and the depositions of J. C. Ballagh, D. G. Miller and E. S. Dulin together [92] with all exhibits thereto, as a part of the record on appeal, said original papers, exhibits and depositions to be held by the Clerk of said Appellate Court pending the appeal herein and to be returned by said Clerk of said Appellate Court to the Clerk of this Court upon the determination of said appeal, unless otherwise provided by the rules of said Appellate Court or by the order of said Appellate Court.

Dated this 7th day of June, 1943.

PAUL J. McCORMICK
United States District Judge

[Endorsed]: Filed June 7, 1943. [93]

[Title of District Court and Cause.]

CERTIFICATE OF CLERK

I, Edmund L. Smith, Clerk of the District Court of the United States for the Southern District of

California, do hereby certify that the foregoing pages numbered from 1 to 93 inclusive contain full, true and correct copies of: Complaint; Notice of Motion to Dismiss on Behalf of Defendants and Each of Them; Minute Order Entered October 27, 1941; Answer to Complaint; Minute Order Entered July 2, 1942; Amendment to Answer; Verification of Complaint; Minute Orders Entered July 3, 1942, July 6, 1942 and July 7, 1942 respectively; Notice of Hearing of Motion to Reopen Case to Admit Newly Discovered Evidence; Petition for Reopening Case to Admit Newly Discovered Evidence; Minute Orders Entered August 17, 1942 and August 31, 1942 respectively; Findings of Fact and Conclusions of Law; Final Judgment; Motion for New Trial; Notice of Motion of Plaintiff for a New Trial and for a Hearing Thereof; Stipulation Concerning Disposition of Motion for New Trial; Minute Orders Entered November 30, 1942 and February 22, 1943 respectively; Letter from Judge Dave W. Ling to Clerk, U. S. District Court; Notice; Notice of Appeal; Cost Bond; Docket Entries; Designation of Contents of Record on Appeal; Stipulation re. record on Appeal and Order re. Transmittal of Original Papers and Exhibits which, together with Original Reporter's Transcript, Original Exhibits and Original Depositions and Exhibits thereto transmitted herewith, constitute the record on appeal to the Circuit Court of Appeals for the Ninth Circuit.

I further certify that my fees for comparing, correcting and certifying the above record amount

to $21.75 which sum has been paid to me by appellant.

Witness my hand and the seal of said District Court this 19 day of June, 1943.

[Seal] EDMUND L. SMITH
Clerk
By THEODORE HOCKE
Deputy Clerk.

[Title of District Court and Cause.]

TESTIMONY

Los Angeles, California
Thursday, July 2, 1942
10:00 o'clock A. M.

The Clerk: Byron Jackson Company v. Patterson-Ballagh Corporation.

Mr. Bednar: Ready for the defendants.

Mr. Lamont: Ready for the plaintiff.

Mr. Bednar: There are a few preliminary matters that I would like to take up first. First, on behalf of the defendant, I would like to file an amendment to our answer. Mr. Lamont has received a copy of it for the plaintiff, and the matter covered in the amendment was taken up in some depositions taken a few months ago.

Mr. Lamont: The only remark I have to make on that is this: Counsel and I have just finished the trial of another case involving the same parties, and if counsel will agree that this will be the last one, I have no objection.

Mr. Bednar: This is the first amendment I have asked for.

Mr. Lamont: Will it be the last one?

Mr. Bednar: We can take that up later. My second motion is that at this time I would like to move to dismiss this action, because the complaint on file herein is not verified under Rule 23(b).

The Court: Well, you can make your motion. Now will someone state the nature of this action?

[2*]

Mr. Lamont: Yes, if your Honor please. I will be as brief as I possibly can. This is a representative suit, where a minority stockholder is suing on behalf of a corporation. Byron Jackson Company owns one-quarter of the outstanding shares of stock of 1,000 shares. We have owned for some years 250 shares of the 1,000, and we are claiming excessive salaries were paid to the executives of the company. I will get to the salaries later. But that is the gist of it, and I don't think there are any more issues except the amount of the salaries.

Mr. Bednar: That is all that I know of.

Mr. Lamont: No question of jurisdiction. Counsel raised the question of diversity of citizenship, that the amount involved is in excess of $3,000, but on the question of diversity of citizenship I think counsel claimed before Judge Yankwich that the question of diversity should depend on the jurisdiction.

Patterson-Ballagh is a defendant, and there are other defendants, and Judge Yankwich ruled in

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* Page numbering appearing at top of page of original Reporter's Transcript.

our favor, that the diversity depends upon the citizenship of the plaintiff, a Delaware corporation, and the other three defendants are residents of California. You have denied one other thing as to jurisdiction, namely, that, according to the rules, it has to be alleged in a suit of this type that it is not collusive, in order to obtain the jurisdiction of this court. I don't know what counsel has in mind in that re- [3] gard, but I think the best answer that I see that it is not collusive is the fact that the three defendants are represented by the same attorney. As to us, I don't know who we could have colluded with in this case. The denial of diversity of citizenship is based upon the contention that the complaint sets forth a derivative action by plaintiff, as a minority stockholder, on behalf of defendant Patterson-Ballagh Corporation, and in California is considered by the California courts to be a trustee for the corporation. And the rule that has been enforced by the federal courts with reference to suits brought by trustees is that for the purpose of diversity of citizenship the citizenship of the trustee is determined by the citizenship of the beneficial interests, and on that basis we claim the plaintiff is trustee for Patterson-Ballagh Corporation, a California corporation, although that corporation is the defendant, and that by reason of that the citizenship of plaintiff is California and the citizenship of the individual defendants is California, and therefore there is no diversity of citizenship.

I am simply going to touch the high points of this case in my opening statement, and if the court wants

to know more about any particular matter I will be glad to answer, if I can.

This is a small corporation, with a capitalization of $200,000. Everything went along very nicely until about the year 1939, when the defendant Miller bought into the com- [4] pany. From then on salaries were raised. We are not making any contention that they are not entitled to a decent salary. In fact, each one is entitled to $1,000 a month. Over that we have our doubts. In 1939 Mr. Miller raised his own salary to $19,750, and in 1939 the salary of Mr. Ballagh was raised to $15,000, and we claim that is $3,000 excessive. In 1940, with no appreciable raise in the earnings of the company, salaries were boosted. Mr. Ballagh in 1940 took $30,166.66 from the company. Mr. Miller also saw that his own salary was boosted to $19,750. In other words, the total of their salaries in 1940 amounted to $49,-916.66, practically $50,000. That was one-quater of the capital. In 1941—and of course we are a little embarrassed, because the bonuses are very largely paid at the end of the year—our action started in September, 1941—but up to that time Mr. Ballagh had taken $16,000 and Mr. Miller had taken $10,500, making a total of $26,500 to September 10th.

We are also going to prove, naturally, the nature of the company. The company owns one plant in Los Angeles, and you might call it a semi-plant in Houston, Texas, and the rest of their activities are simply of the nature of sales agencies. The number of employees ranged from 25 to 35. We are not

dealing with a large company. It is a small company, that had no financial problems at all. They had nothing specially to supervise. It is a manufacturing company manufacturing a specialty, and the difficulties of manage- [5] ment should not be very great.

In addition to that, the majority of holders of the stock owned three-quarters and we owned one-quarter. In February of 1939 Mr. Miller came in. He did three things which are most significant here. He first of all stopped our dividends. We haven't had a dividend since. He boosted salaries, as I have shown, and, besides that, we had a royalty agreement with the company which was paying us about $18,000 a year, and the agreement was repudiated. That is in litigation in Judge Hollzer's court. In other words, it was a question of getting money out of the company in some way that doesn't benefit us, and that is the reason we come before this court here.

There are five directors on the board. Mr. Dulin, who is president of the Byron Jackson Company, represented the minority, and the other four directors consist of the two defendants, Mr. Burrell, who is attorney for the defendant company, and an employee of the company, and we were outnumbered four to one in the directorship. We were also outnumbered in stock, so we didn't have very much to say about the management of the organization.

These salaries were increased at a time when the earnings would not warrant it, and, as far as I

know, nothing warranted it. In 1940 the increase was made on a company statement which turned out to be inaccurate, and we are going to prove that by the company's auditor later on. Instead of large earnings in 1940, on which the [6] raises were based, they amounted to something like $50,000. And in 1941, there were profits of about the same type, just about the same comparison, about $50,000. So this was protested against by us. I will say very frankly that we believe a stockholder in a company should get some recognition, and that is the reason we are in court here.

Mr. Bednar: I just want to make a very short answer. In the first place, the statements that counsel for plaintiff has made are quite general; that, for instance, Mr. Miller, during a period of time—the important period of time in this case is from approximately January 1, 1939, to September 10, 1941, when the action was filed—that during 1939, Mr. Miller, for example, drew $1,000 a month, and in March of 1940 we will show that Mr. Miller, at a board meeting at which Mr. Dulin was present, was voted $1500 a month, and Mr. Miller has been drawing that $1500 a month until September 10, 1941, at the time this action was filed.

In Mr. Ballagh's case, Mr. Ballagh was likewise voted $2,000 a month at the same meeting, the same meeting at which Mr. Miller received the $1500 a month. Mr. Dulin objected to Mr. Ballagh drawing the raised compensation. We feel that we will show that Mr. Dulin was not sufficiently acquainted

with the affairs of the defendant corporation, that he spent practically not time, on an annual basis, discussing the problems of the defendant corporation with the officers and directors, and that he made no objection to the [7] salaries until after the patent license agreement had been repudiated by the defendant corporation in the other suit in Judge Hollzer's court. Prior to that time it was perfectly agreeable, but after that time he made the objections. We will show that, despite these objections which they have had to salaries, Mr. Dulin at every meeting at which he was present, at which directors were elected, voted for the same directors, knowing their ideas on compensation, and that he, as one of the directors, voted for the same officers at every meeting at which he was present and at which officers were elected.

We will show, furthermore, that in October 1938, just about two or three months prior to the period in question, that Mr. Dulin voted, in fact moved, that Mr. Ballagh be paid $1500 a month for performing the duties that he performed during the period of time in question, and that Mr. Dulin at the time moved that Mr. Patterson, who was the predecessor of Mr. Miller and performed the same duties that Mr. Miller was performing, that Mr. Dulin voted that Mr. Patterson get $1500. In October, 1938, Mr. Dulin thought $1500 was enough compensation.

On the subject of whether or not the company's statement was correct, we believe the evidence will show that the company's statement was announced

to be tentative, and that plaintiff should have known, at any rate, that there were certain items, consisting of reserves for contingent lia- [8] bilities, as to which no attempt was made to set them up on these statements, and that the final audit of the year, and which was put out by certified public accountants, was to be the final document, and that the others were a tentative indication of how the business was going, and we will show various factors in justification of the salaries these men were receiving. One of those factors is, of course, the duties these men have been performing, and the time they have spent in working for the corporation. And we will show that they performed very valuable functions, notably in the field of invention.

I believe we will be able to show that, while Mr. Lamont refers to it as being a very small business, that it is a very important business. It has to do with the selling of rubber specialties in the field of oil tools. The business itself is of a limited nature and very uncertain, and must depend upon the patent aspects of the corporation and its ability to keep abreast of the trade.

Mr. Lamont: There is one correction that I want to make. Mr. Bednar said that I said 1929 when I should have said 1939, and the other is that the company is capitalized for $100,000 and not $200,000.

Mr. Bednar: Not the stated capital but the entire capital of the company.

Mr. Lamont: Have you a copy of the minute book?

Mr. Bednar: I don't have a copy. I have the minute [9] book.

Mr. Lamont: I am only going to put in Section 3 of Article III, salaries. All I care about is one section. I am going to keep the record as short as possible.

Section 3 of Article III of the By-Laws reads as follows: "The officers may receive only such salaries as the Board of Directors may from time to time determine. Until the salary of an officer has been fixed by resolution of the Board of Directors, such officer shall serve without compensation."

[10]

I point that out to show that there is no carte-blanche in these by-laws as to fixing salaries, and as I pointed out, it is an instance of directors dealing with themselves. In a case of that kind the burden of proof is not on us; it is really on the directors who fix their own salaries. I think the real principle of law is as I have stated it.

I might state to the court that Mr. Patterson was one of the original founders of this business, he and Mr. Ballagh, and Mr. Patterson sold out to Mr. Miller, and that is when our trouble started.

I would like to offer in evidence the minutes of the company attached to the depositions, which means from the 1st day of October, 1936, up to the time of filing this suit.

Mr. Bednar: I haven't had a chance to check this at all, but I am perfectly agreeable to it going in.

Mr. Lamont: I want to read a few things from

the minutes, if the court will indulge me. I refer to the minutes of January 29, 1937. I will say to start with that we were opposed to some of their salaries before Mr. Miller came in, but not at all to the extent that we were afterwards, and we consistently objected to the amounts the officers were drawing for some years back. For instance, in this meeting of January 27, 1937, it is said:

> "Upon motion duly made and seconded the following Resolution was adopted: [11]
>
> "Be It Resolved, that the salaries prevailing for the past year of the two executive officers are hereby approved.
>
> "Mr. Patterson and Mr. Ballagh voted in the affirmative, and Mr. Dulin voted in the negative, on the foregoing resolution.
>
> "Mr. Dulin stated that, in his opinion, from the preliminary financial statement rendered the company's financial condition has not allowed the administrative salaries being paid which, in his opinion, are excessive, and further, the dividends declared during the year should not have been paid."

It isn't a question of Byron Jackson trying to cripple this company by asking for dividends. This very statement shows that he wanted the company to get along, but he didn't like to have it taken out in salaries.

> "Taking into consideration the condition of the business, the volume of sales, as a director and a stockholder, he urged that the administrative salaries be adjusted downward and that

no further dividends be paid until the company is in a greatly improved financial position."

Mr. Bednar: Are these exhibits to receive an exhibit number?

Mr. Lamont: I think so. I am introducing them at this [12] time.

The Clerk: Let me mark that book, then.

Mr. Lamont: They are part of the depositions.

Mr. Bednar: What is the date of the minutes?

Mr. Lamont: They run from October 1, 1936, up to the time of the filing of this suit, and they were supplied by counsel, so I assume they are correct.

The Clerk: That will be Plaintiff's Exhibit 1.

PLAINTIFF'S EXHIBIT No. 1

APPENDIX

Copies of Minutes Appearing in Minute Books of Patterson-Ballagh Corporation, Commencing October 1, 1936, and Up to September 10, 1941.

CALL AND WAIVER OF NOTICE OF SPECIAL MEETING OF BOARD OF DIRECTORS OF PATTERSON-BALLAGH CORPORATION, LTD.

We, the undersigned, being all of the Directors of Patterson-Ballagh Corporation, Ltd., desiring to hold a special meeting of the Board of Directors of said corporation, hereby give our written consent

Plaintiff's Exhibit No. 1—(Continued)

to the holding of a special meeting of the said Board for October 1, 1936, at 11:00 o'clock a.m. of the said date, in the offices of Byron Jackson Company at 2150 East Slauson Avenue, Los Angeles, California, for the purpose of transacting such business as may come before the meeting, and we hereby waive all notice of such meeting and consent to the holding thereof.

And we do further agree that any and all business transacted at said meeting shall be as valid and legal and of the same force and effect as though said meeting were held after notice otherwise duly given, served and published, and we hereby waive notice and publication of notice of the time and place of such meeting of the Board of Directors of said Corporation.

Witness our hand this first day of October, 1936.

(Sgd) C. L. PATTERSON,
(Sgd) E. S. DULIN,
(Sgd) J. C. BALLAGH,
Directors.

MINUTES OF SPECIAL MEETING OF BOARD OF DIRECTORS OF PATTERSON-BALLAGH CORPORATION, LTD.

A special meeting of the Board of Directors of Patterson-Ballagh Corporation, Ltd., was held on the 1st day of October, 1936, at 11:00 o'clock a.m. in the offices of Byron Jackson Company, 2150 East

Plaintiff's Exhibit No. 1—(Continued)

Slauson Avenue, Los Angeles, California, there being present and acting at said meeting

J. C. Ballagh
E. S. Dulin
C. L. Patterson

being all of the directors of said corporation.

The meeting was called to order by Mr. C. L. Patterson, and Mr. J. C. Ballagh acted as Secretary.

The minutes of the last meeting were read and approved on motion duly made, seconded and unanimously carried.

The Secretary then presented to the meeting the original waiver of notice and consent to the meeting, signed by all of the directors, which waiver of notice was, upon motion duly made and carried, ordered to be made a part of the records of this meeting and entered in the Minute Book on the page immediately preceding the minutes of this meeting.

The President announced that the meeting was called for the purpose of ratifying the acts of the officers in declaring dividends as of August 1, 1936 and September 1, 1936.

Upon motion duly made, seconded and carried, the following Resolution was unanimously adopted:

> Resolved: That the Board of Directors do and they hereby ratify the acts of the officers in declaring a dividend of two (2) per cent, declared as of August 1, 1936, and paid August 25, 1936, out of the profits of the corporation

Plaintiff's Exhibit No. 1—(Continued)

earned prior to August 1, 1936, as shown by the financial report of August 1, 1936.

Resolved Further: That the Board of Directors do and they hereby ratify the acts of the officers in declaring a dividend of two (2) per cent, declared as of September 1, 1936, and paid September 30, 1936, out of the profits of the corporation earned prior to September 1, 1936, as shown by the financial report of September 1, 1936.

Upon motion of Mr. Dulin, seconded by Mr. Patterson, and unanimously carried, the following Resolution was adopted:

Resolved: That the meetings of the Board of Directors be not held on less than three (3) days' notice in writing by mail to each director.

Upon motion of Mr. Patterson, seconded by Mr. Ballagh, the following Resolution was adopted:

Resolved: That the Board of Directors fix the salaries of C. L. Patterson, President, and J. C. Ballagh, Secretary-Treasurer, at $1250.00 each per month effective as of August 1, 1936, and $2,000.00 each per month effective as of September 1, 1936.

Mr. Patterson and Mr. Ballagh voted in the affirmative, and Mr. Dulin voted in the negative, on the foregoing Resolution.

Mr. Dulin stated that, in his opinion, the administrative costs were out of all proportion to the

Plaintiff's Exhibit No. 1—(Continued)

volume of business transacted by Patterson-Ballagh Corporation, Ltd.

There being no further business to come before the meeting, on motion duly made, seconded and carried, it was thereupon adjourned.

(Sgd) C. L. PATTERSON,
President.

(Sgd) J. C. BALLAGH,
Secretary.

(Sgd) C. L. PATTERSON,

(Sgd) E. S. DULIN.

Mr. Patterson and Mr. Ballagh voted in the affirmative, and Mr. Dulin voted in the negative, on the foregoing Resolution.

Mr. Dulin stated that, in his opinion, the administrative costs were out of all proportion to the volume of business transacted by Patterson-Ballagh Corporation, Ltd.

There being no further business to come before the meeting, on motion duly made, seconded and carried, it was thereupon adjourned.

(Sgd) C. L. PATTERSON.

(Sgd) J. C. BALLAGH,
Secretary.

(Sgd) C. L. PATTERSON,

(Sgd) J. C. BALLAGH,

(Sgd) E. S. DULIN,
Directors.

Plaintiff's Exhibit No. 1—(Continued)

CALL AND WAIVER OF NOTICE OF SPECIAL MEETING OF BOARD OF DIRECTORS OF PATTERSON-BALLAGH CORPORATION, LTD.

We, the undersigned, being all of the Directors of Patterson-Ballagh Corporation, Ltd., desiring to hold a special meeting of the Board of Directors of said corporation, hereby give our written consent to the holding of a special meeting of the said Board for December 28, 1936, at 3:00 o'clock p.m. of the said date, in the offices of Byron Jackson Company at 2150 East Slauson Avenue, Los Angeles, California, for the purpose of adopting a Resolution authorizing the borrowing of $6700.00 from the Security-First National Bank of Los Angeles, to be covered by Trust Deed on real estate and buildings, and for the purpose of transacting such business as may come before the meeting, and we hereby waive all notice of such meeting and consent to the holding thereof.

And we do further agree that any and all business transacted at said meeting shall be as valid and legal and of the same force and effect as though said meeting were held after notice otherwise duly given, served and published, and we hereby waive notice and publication of notice of the time and place of such meeting of the Board of Directors of said corporation.

Plaintiff's Exhibit No. 1—(Continued)

Witness our hand this twenty-eighth day of December, 1936.

(Sgd) J. C. BALLAGH,
(Sgd) C. L. PATTERSON,
(Sgd) E. S. DULIN,
Directors.

MINUTES OF SPECIAL MEETING OF BOARD OF DIRECTORS OF PATTERSON-BALLAGH CORPORATION, LTD.

A special meeting of the Board of Directors of Patterson-Ballagh Corporation, Ltd. was held on the 28th day of December, 1936, at 3:00 o'clock p.m. in the offices of Byron Jackson Company, 2150 East Slauson Avenue, Los Angeles, California, there being present and acting at said meeting

J. C. Ballagh
E. S. Dulin
C. L. Patterson

being all of the directors of said corporation.

The meeting was called to order by Mr. C. L. Patterson, and Mr. J. C. Ballagh acted as Secretary.

The minutes of the last meeting were read and approved on motion duly made, seconded and unanimously carried.

The Secretary then presented to the meeting the original waiver of notice and consent to the meeting, signed by all of the directors, which waiver

Plaintiff's Exhibit No. 1—(Continued)

of notice was, upon motion duly made and carried, ordered to be made a part of the records of this meeting and entered in the Minute Book on the page immediately preceding the minutes of this meeting.

The President announced that the meeting was called for the purpose of passing a Resolution authorizing the corporation to borrow $6700.00 from the Security-First National Bank of Los Angeles, California.

Upon motion duly made, seconded and carried, the following Resolution was unanimously adopted:

> Resolved: That Patterson-Ballagh Corporation, Ltd. borrow from the Security-First National Bank of Los Angeles, California, the sum of $6700.00, to be covered by Trust Deed on the following described property:
>
> Lots One (1), Two (2), the West 70 feet of Lot Three (3), all of Lots Twenty-four (24) and Twenty-five (25) of Tract Number Six (6), being a resubdivision of certain lots in E. B. Grandins Subdivision, in the County of Los Angeles, State of California, as per map recorded in Book 12, page 174 of Maps, in the office of the County Recorder of said County.

There being no further business to come before

Plaintiff's Exhibit No. 1—(Continued)

the meeting, on motion duly made, seconded and carried, it was thereupon adjourned.

(Sgd) C. L. PATTERSON,
President.

(Sgd) J. C. BALLAGH,
Secretary.

(Sgd) C. L. PATTERSON,
(Sgd) J. C. BALLAGH,
(Sgd) E. S. DULIN,
Directors.

(Document next bound in Minute Book is as follows:)

(Endorsed:) Triplicate
Resolution to Borrow
Money—To Give Security

Patterson-Ballagh Corporation, Ltd.
A Corporation
to
Security-First National
Bank of Los Angeles

Dated December 23rd, 1936
Certified Copy of
Resolution to Borrow Money—To Give Security
(Real Estate)

(1) Resolved, that this corporation Patterson-Ballagh Corporation, Ltd., will borrow from the Security-First National Bank of Los Angeles, the sum of Sixty-Seven Hundred.....Dollars;

(2) Whereas, this corporation Patterson-Ballagh Corporation, Ltd. (initials in ink:) JCB has

Plaintiff's Exhibit No. 1—(Continued)

duly and regularly borrowed from the Security-First National Bank of Los Angeles, the sum of Eight Hundred.....Dollars;

To evidence said debt this corporation will execute its promissory note in favor of said bank under date of December 23rd, 1936, for the term of 5 years, payable in installments, with interest at 6 per cent per annum, payable monthly; Monthly installments of $75.00 each, including interest commencing January 23, 1937, balance due Dec. 23, 1941, and to secure the payment thereof, and of any renewals or extensions thereof, will execute its mortgage or trust deed affecting the following described property:

Lots One (1), Two (2), the West 70 feet of Lot Three (3), all of Lots Twenty-four (24) and Twenty-five (25) of Tract Number Six (6), being a resubdivision of certain lots in E. B. Grandins Subdivision, in the County of Los Angeles, State of California, as per map recorded in Book 12, Page 174 of Maps in the office of the County Recorder of said County.

and will include in said mortgage or trust deed, or will now and/or will from time to time execute as separate instruments, assignments of such leases, mortgages on such personal property, and/or pledges of such other security therefor as said bank shall require; said (c.—note and) mortgage, trust deed, assignments of leases, chattel mortgages or pledge agreements to be in the form used or ap-

Plaintiff's Exhibit No. 1—(Continued)

proved by and upon such terms as may be arranged for with said bank, including conditions as to default, suit and attorneys' fees, management of property and distribution of income.

Resolved further that C. L. Patterson, the President, and J. C. Ballagh, the Secretary, of this corporation, be, and they are hereby authorized, empowered, and directed to make, execute and deliver the instruments hereinbefore mentioned, and such other instruments in connection therewith as may be agreed upon between them and said bank, in the name of and as the act and deed of this corporation, and is hereby appointed and authorized as the agent of this corporation to execute on its behalf the affidavit of good faith required on any chattel mortgage executed by this corporation as mortgagor.

I, J. C. Ballagh, Secretary of the Patterson-Ballagh Corporation, Ltd., hereby certify that the foregoing is a true copy of a resolution duly and legally adopted by the Board of Directors of said corporation, at a legal meeting of said Board duly and regularly held on the 28th day of December, A.D., 1936, and that said resolution has not been revoked.

Plaintiff's Exhibit No. 1—(Continued)

In Witness Whereof, I have hereunto set my hand and affixed the corporate seal of said corporation this 28th day of December, A.D., 1936.

(Sgd) J. C. BALLAGH,
Secretary.

[Corporate Seal]

Mc:ED

CALL AND WAIVER OF NOTICE OF SPECIAL MEETING OF STOCKHOLDERS OF PATTERSON-BALLAGH CORPORATION, LTD.

We, the undersigned, being all of the stockholders of Patterson-Ballagh Corporation, Ltd., desiring to hold a special meeting of the stockholders of said corporation, hereby give our written consent to the holding of a special meeting of the said stockholders for January 29, 1937, at 11:00 o'clock a. m. of the said date, in the offices of Byron Jackson Company, at 2150 East Slauson Avenue, Los Angeles, California, for the purpose of discussing such matters as may come before the meeting.

And we do further agree that any and all business transacted at said meeting shall be as valid and legal and of the same force and effect as though said meeting were held after notice otherwise duly given, served and published, and we hereby waive notice and publication of notice of the time and place of such meeting of the stockholders of said corporation.

Plaintiff's Exhibit No. 1—(Continued)

Witness our hands this 29th day of January, 1937.

(Sgd) C. L. PATTERSON,
C. L. Patterson.

(Sgd) J. C. BALLAGH,
J. C. Ballagh.

(Sgd) E. S. DULIN,
Byron Jackson Co.,
(A corporation by E. S. Dulin, President.)

(Sgd) J. C. BALLAGH,
Highland Investment Corp, Ltd.

(By J. C. Ballagh, President.)

(Sgd) E. S. DULIN,
E. S. Dulin.
Stockholders.

MINUTES OF ANNUAL MEETING OF STOCKHOLDERS OF PATTERSON-BALLAGH CORPORATION, LTD.

The annual meeting of the stockholders of Patterson-Ballagh Corporation, Ltd., was held in the offices of Byron Jackson Company, 2150 East Slauson Avenue, Los Angeles, California, on January 29, 1937, at 11:00 o'clock a. m.

Plaintiff's Exhibit No. 1—(Continued)

The meeting was called to order by President C. L. Patterson, who acted as Chairman of the meeting, and Mr. J. C. Ballagh acted as Secretary.

Secretary J. C. Ballagh presented to the meeting the original waiver of notice and consent to the meeting, signed by all of the stockholders, which waiver of notice was, upon motion duly made and carried, ordered to be made a part of the records of this meeting and entered in the Minute Book on the page immediately preceding the minutes of this meeting.

The Secretary thereupon called the roll of stockholders and the following report was made of stockholders and stock representatives at the meeting:

Name	No. of Shares
Ballagh, J. C.	125
Byron Jackson Company, (a corporation, by E. S. Dulin, President)	249
Dulin, E. S.	1
Highland Investment Corp, Ldt., by J. C. Ballagh, President	250
Patterson, C. L.	375
Total Capital Stock	1,000

The Secretary reported that the above number of shares represented all of the issued and outstanding stock as of said date.

The financial report of the corporation for the

Plaintiff's Exhibit No. 1—(Continued)

period ending December 31, 1936, as prepared under the direction of the Secretary-Treasurer, was presented and unanimously approved and a summary of same was ordered attached hereto and made a part of the minutes of this meeting.

Upon motion duly made, seconded and carried, the following Resolution was unanimously adopted:

> Be It Resolved, that each and every act of the directors of this corporation, and of each of the officers of this corporation, as shown by the records of this corporation, with the exception of the officers' salaries, and also with the exception of any acts of the officers expressly disapproved by the Board of Directors of this corporation, be and the same are hereby ratified, adopted, approved and confirmed, as and for the acts of this corporation.

Upon motion duly made and seconded the following Resolution was adopted:

> Be It Resolved, that the salaries prevailing for the past year of the two executive officers are hereby approved.

Mr. Patterson and Mr. Ballagh voted in the affirmative, and Mr. Dulin voted in the negative, on the foregoing resolution.

Mr. Dulin stated that, in his opinion, from the preliminary financial statement rendered the company's financial condition has not allowed the administrative salaries being paid which, in his opinion, are excessive, and further, the dividends de-

Plaintiff's Exhibit No. 1—(Continued)

clared during the year should not have been paid. Taking into conisderation the condition of the business, the volume of sales, as a director and a stockholder, he urged that the administrative salaries be adjusted downward and that no further dividends be paid until the company is in a greatly improved financial position.

The Chairman announced that the next business before the meeting was the election of a Board of Directors for the ensuing year. Thereupon, the following were duly nominated as directors to serve until the next annual election and until the election and qualification of their respective successors:

Ballagh, J. C.
Dulin, E. S.
Patterson, C. L.

There being no further business to come before the meeting, on motion duly made, seconded and carried, it was thereupon adjourned.

(Sgd) C. L. PATTERSON,
Chairman.

(Sgd) J. C. BALLAGH,
Secretary.

Plaintiff's Exhibit No. 1—(Continued)

Secretary's Report of 1936 Operations

INCOME and PROFIT and LOSS

Gross Sales		$191,546.95
Cost of Goods Sold		46,342.91
		145,204.04
Operating Expenses		125,123.26
Net Operating Profit		20,080.78
Other Expenses—Less Other Income		4,231.54
Net Gain for period		15,849.24

Summary of Surplus

Balance as per Ledger 12/31/35		$ 75,044.16
1936 Credits:		
Adjustment of Depreciation as per Federal Tax Investigation on 1934-1935 Returns	5,625.65	
Net Profit from Operations	15,849.24	21,474.89
		$ 96,519.05
1936 Charges:		
Capital Stock Tax 1935	350.00	
Federal Income Tax and Excess Profit Tax	842.78	
Dividends Declared 2/25/36	2,000.00	
" " 8/ 1/36	2,000.00	
" " 9/ 1/36	2,000.00	
	6,000.00	7,192.78
Surplus Balance 12/31/36		$ 89,326.27

I, J. C. Ballagh, as Secretary-Treasurer of Patterson-Ballagh Corporation, Ltd., hereby certify that the foregoing report is true, to the best of my knowledge and belief.

(Sgd) J. C. BALLAGH
J. C. Ballagh

Plaintiff's Exhibit No. 1—(Continued)

CALL AND WAIVER OF NOTICE OF SPECIAL MEETING OF BOARD OF DIRECTORS OF PATTERSON-BALLAGH CORPORATION, LTD.

We, the undersigned, being all of the Directors of Patterson-Ballagh Corporation, Ltd., desiring to hold a special meeting of the Board of Directors of said corporation, hereby give our written consent to the holding of a special meeting of the said Board for January 29, 1937, at 11:00 o'clock a. m. of said date, in the offices of Byron Jackson Company, at 2150 East Slauson Avenue, Los Angeles, California, for the purpose of discussing such matters as may come before the meeting.

And we do further agree that any and all business transacted at said meeting shall be as valid and legal and of the same force and effect as though said meeting were held after notice otherwise duly given, served and published, and we hereby waive notice and publication of notice of the time and place of such meeting of the Board of Directors of said corporation.

Witness our hands this 29th day of January, 1937.

(Sgd) C. L. PATTERSON,
C. L. Patterson.
(Sgd) J. C. BALLAGH,
J. C. Ballagh.
(Sgd) E. S. DULIN,
E. S. Dulin.
Directors.

Plaintiff's Exhibit No. 1—(Continued)

MINUTES OF ANNUAL MEETING OF DIRECTORS OF PATTERSON-BALLAGH CORPORATION, Ltd.

The annual meeting of directors of Patterson-Ballagh Corporation, Ltd., was held in the offices of Byron Jackson Company, 2150 East Slauson Avenue, Los Angeles, California, on January 29, 1937, immediately following the annual meeting of the stockholders.

There were present and acting at said meeting:

J. C. Ballagh
E. S. Dulin
C. L. Patterson

being all of the directors of said corporation.

The meeting was called to order by Mr. E. S. Dulin, who acted as Chairman of the meeting, and Mr. J. C. Ballagh acted as Secretary.

Secretary J. C. Ballagh presented to the meeting the original waiver of notice and consent to the meeting, signed by all of the directors, which waiver of notice was, upon motion duly made and carried, ordered to be made a part of the records of this meeting and entered in the Minute Book on the page immediately preceding the minutes of this meeting.

The Chairman stated that the first business to come before the meeting was the election of officers for the ensuing year, and the following persons were nominated for the respective offices, to-wit:

Plaintiff's Exhibit No. 1—(Continued)

C. L. Patterson, President
J. C. Ballagh, Secretary-Treasurer

There being no further nominations, and the nominations of the above named persons being duly seconded, a vote was had and the Secretary declared the said persons unanimously nominated for the said respective offices for the ensuing year.

There being no further business to come before the meeting, on motion duly made, seconded and carried, it was thereupon adjourned.

(Sgd) E. S. DULIN,
E. S. Dulin, Chairman.
(Sgd) J. C. BALLAGH,
J. C. Ballagh.

(Sgd) J. C. BALLAGH,
J. C. Ballagh.
(Sgd) E. S. DULIN,
E. S. Dulin.
(Sgd) C. L. PATTERSON,
C. L. Patterson.
Directors.

CALL AND WAIVER OF NOTICE OF SPECIAL MEETING OF BOARD OF DIRECTORS OF PATTERSON-BALLAGH CORPORATION, Ltd.

We, the undersigned, being all of the Directors of Patterson-Ballagh Corporation, Ltd., desiring to hold a special meeting of the Board of Directors of said corporation, hereby give our written con-

Plaintiff's Exhibit No. 1—(Continued)

sent to the holding of a special meeting of the said Board for March 31, 1937, at 11 o'clock a. m. of the said date, in the offices of Byron Jackson Company at 2150 East Slauson Avenue, Los Angeles, California, for the purpose of transacting such business as may come before the meeting, and we hereby waive all notice of such meeting and consent to the holding thereof.

And we do further agree that any and all business transacted at said meeting shall be as valid and legal and of the same force and effect as though said meeting were held after notice otherwise duly given, served and published, and we hereby waive notice and publication of notice of the time and place of such meeting of the Board of Directors of said Corporation.

Witness our hand this 31st day of March, 1937.

(Sgd) J. C. BALLAGH,
J. C. Ballagh.

(Sgd) E. S. DULIN,
E. S. Dulin,

(Sgd) C. L. PATTERSON,
C. L. Patterson.

MINUTES OF SPECIAL MEETING
OF
BOARD OF DIRECTORS OF
PATTERSON-BALLAGH CORPORATION, Ltd.

A special meeting of the Board of Directors of

Plaintiff's Exhibit No. 1—(Continued)

Patterson-Ballagh Corporation, Ltd., was held on the 31st day of March, 1937, at 11:00 o'clock a. m. in the offices of Byron Jackson Company, 2150 East Slauson Avenue, Los Angeles, California, there being present and acting at said meeting

J. C. Ballagh
E. S. Dulin
C. L. Patterson

being all of the directors of said corporation.

The meeting was called to order by Mr. C. L. Patterson, who acted as Chairman.

The minutes of the last meeting were read and approved on motion duly made, seconded and unanimously carried.

The Secretary then presented to the meeting the original waiver of notice and consent to the meeting, signed by all of the directors, which waiver of notice was, upon motion duly made and carried, ordered to be made a part of the records of this meeting and entered in the Minute Book on the page immediately preceding the minutes of this meeting.

The Secretary announced that the meeting was called for the purpose of passing on the advisability of establishing a line of credit with the Security-First National Bank of Los Angeles, in the amount of $15,000.00, by pledging the Accounts Receivable of the Corporation.

After a general discussion of the subject, and in view of Director Dulin's opinion in the matter, the Resolution as offered was withdrawn without having been voted upon.

Plaintiff's Exhibit No. 1—(Continued)

The next matter to come up for discussion was the establishment of a group, composed of a committee of five, to assist in the operation of Patterson-Ballagh Corporation's affairs, substantially as outlined in the attached memorandum, which was confirmed by the Board.

There being no further business to come before the meeting, on motion duly made, seconded and carried, it was thereupon adjourned.

(Sgd) C. L. PATTERSON,
C. L. Patterson, Chairman.

(Sgd) J. C. BALLAGH,
J. C. Ballagh, Secretary.

(Sgd) C. L. PATTERSON,

(Sgd) J. C. BALLAGH,

(Sgd) E. S. DULIN,
Directors.

MEMORANDUM OF AGREEMENT

between

J C BALLAGH and C L PATTERSON

An agreement has been reached as to the conduct of Patterson-Ballagh Corporation in matters other than those normally carried before the Board.

1. A committee of 5 to act on all matters concerning the operation of the business, consisting of the following:

Plaintiff's Exhibit No. 1—(Continued)

J C Ballagh
C L Patterson
W W Cahoon (Office)
R A McWaid (Factory)
P A Medearis (Sales)

2. Meetings to be held each and every Monday at 11:00 o'clock a. m.; any member of the group unable to attend is to appoint a substitute who is to act for him. Meeting called to order by a temporary Chairman (J. C. Ballagh, if present) with a secretary to take notes of the meeting. At first meeting a permanent Chairman to be voted on and after the first meeting the notes of the previous meeting to be read. All matters brought before the group to be read into the records, which are to be available to all members, with copies of the minutes of the various meetings to be sent to each Director.

Matters to be presented on motion and to be seconded and voted on under regular rule of order. After vote the majority rule to be agreed upon without further argument or hard feelings. In the event of a deadlock or refusal of a member to accede to the majority rule the matter to be brought before the Board of Patterson-Ballagh Corporation and the decision of the Board to be final.

3. The matters to be brought before the group are those of current problems and reports of the actions of members that were given specific instructions in the previous meetings; also, any report of emergency action that has been take since the last meeting.

4. Any action as passed and approved by the

Plaintiff's Exhibit No. 1—(Continued)

group is considered normal and acts as a basis for future operations when the same action arises between meetings.

5. Any emergency action taken by members of the group between meetings to be according to best judgment and to be accepted by the group as being for the best interest of the corporation; no member to be censored for making a decision that is considered wrong by the group. The group, however, has the right to pass a resolution correcting the matter insofar as possible.

March 25, 1937.

MINUTES OF SPECIAL MEETING
OF
BOARD OF DIRECTORS OF PATTERSON-BALLAGH CORPORATION, Ltd.

A special meeting of the Board of Directors of Patterson-Ballagh Corporation, Ltd. was held on the 17th day of May, 1937, at 11:00 o'clock a. m. in the offices of the corporation at 1900 East 65th Street, Los Angeles, California, pursuant to notice issued.

There were present and acting at said meeting

J. C. Ballagh

C. L. Patterson

Director E. S. Dulin was absent.

The meeting was called to order by Mr. J. C. Ballagh who acted as Chairman.

The minutes of the last meeting were read and

Plaintiff's Exhibit No. 1—(Continued)

approved on motion duly made, seconded and unanimously carried.

The Chairman announced that the first thing to come before the meeting was the matter of securing a permit for the corporation to do business in the states of Louisiana and Texas, and upon motion duly made and seconded it was unanimously

Resolved, That Patterson-Ballagh Corporation, Ltd. make application for permit to do business in the State of Louisiana;

Resolved Further, That Fred. Bennett, Box 23, Oil City, Louisiana, be appointed Resident Agent.

Resolved, That Patterson-Ballagh Corporation, Ltd. make application for permit to do business in the State of Texas;

Resolved Further, That J. M. O'Melveny, 2127 Bartlett Street, Houston, Texas, be appointed Resident Agent.

Resolved, That any papers or affidavits made out in connection with securing the permits, referred to in the foregoing resolutions, be submitted to Mr. F. Ewing for approval before being filed.

The Chairman then stated that the next thing to come before the Board was the approval of a recommended change in the selling method in the Mid-Continent, whereby we would sell through approved dealers only, together with a change in the discount allowed, and the elimination of the 2 per cent cash discount previously allowed to the entire trade.

Plaintiff's Exhibit No. 1—(Continued)

Upon motion duly made and seconded, it was unanimously

Resolved, That a letter be sent to all supply stores through which we have sold in the past, withdrawing all discounts effective June 1st;

Resolved Further, That we send a letter to an approved list of dealers notifying them of their re-instatement and advising that effective June 1st the new discount will be 10 per cent for non-stocking jobbers, and 15 per cent for those stocking our merchandise;

Resolved Further, That the entire trade be notified of the withdrawal of the 2 per cent cash discount previously allowed.

The next matter that came up for discussion was the propsed establishment of a bonus for Mr. J. M. O'Melveny and the Mid-Continent employes; also a salary increase for Mr. O'Melveny. Upon motion duly made and seconded, it was unanimously

Resolved, That a fair and adequate bonus system be established within the next month that will pay a percentage over the salary now being made to Mr. J. M. O'Melveny and the men under him;

Resolved Further, That Mr. O'Melveny be granted a salary increase of $50.00 per month.

There being no further business to come before

Plaintiff's Exhibit No. 1—(Continued)

the meeting, on motion duly made, seconded and carried, it was thereupon adjourned.

(Sgd) C. L. PATTERSON
President

(Sgd) J. C. BALLAGH
Secretary

(Sgd) J. C. BALLAGH
J. C. Ballagh

(Sgd) C. L. PATTERSON
C. L. Patterson

CALL AND WAIVER OF NOTICE OF SPECIAL MEETING OF BOARD OF DIRECTORS OF PATTERSON-BALLAGH CORPORATION, Ltd.

We, the undersigned, being all of the Directors of Patterson-Ballagh Corporation, Ltd., desiring to hold a special meeting of the Board of Directors of said corporation, hereby give our written consent to the holding of a special meeting of the said Board for October 27, 1937, at 11 o'clock a. m. of the said date, in the offices of Byron Jackson Company at 2150 East Slauson Avenue, Los Angeles, California, for the purpose of transacting such business as may come before the meeting, and we hereby waive all notice of such meeting and consent to the holding thereof.

And we do further agree that any and all business transacted at said meeting shall be as valid and legal and of the same force and effect as though

Plaintiff's Exhibit No. 1—(Continued)

said meeting were held after notice otherwise duly given, served and published, and we hereby waive notice and publication of notice of the time and place of such meeting of the Board of Directors of said corporation.

Witness our hand this twenty-seventh day of October, 1937.

(Sgd) C. L. PATTERSON
(Sgd) J. C. BALLAGH
(Sgd) E. S. DULIN
Directors

MINUTES OF SPECIAL MEETING OF BOARD OF DIRECTORS OF PATTERSON-BALLAGH CORPORATION, Ltd.

A special meeting of the Board of Directors of Patterson-Ballagh Corporation, Ltd. was held on the 27th day of October, 1937, at 11:00 o'clock a. m., in the offices of Byron Jackson Co., at 1250 East Slauson Avenue, Los Angeles, California, there being present and acting at said meeting

J. C. Ballagh
E. S. Dulin
C. L. Patterson

being all of the directors of said corporation.

The meeting was called to order by Mr. C. L. Patterson, who acted as Chairman.

The minutes of the last meeting were read and approved on motion duly made, seconded and unanimously carried.

Plaintiff's Exhibit No. 1—(Continued)

The Secretary then presented to the meeting the original waiver of notice and consent to the meeting, signed by all of the directors, which waiver of notice was, upon motion duly made and carried, ordered to be made a part of the records of this meeting and entered in the Minute Book on the page immediately preceding the minutes of this meeting.

A discussion was had relative to the form in which the financial reports were prepared, and it was suggested by Mr. Dulin that the report show a surplus carried ahead month by month. It was decided by the Board to carry on with the present system of auditing until the first of the year and possibly at that time consider a good man in the organization in the place of an outside auditor.

It was unanimously agreed that the matter of payment of bonuses to employees would be discussed at a meeting to be called during the first part of December.

There being no further business to come before the meeting, on motion duly made, seconded and carried, it was thereupon adjourned.

(Sgd) C. L. PATTERSON
Chairman

(Sgd) J. C. BALLAGH
Secretary

(Sgd) C. L. PATTERSON
(Sgd) J. C. BALLAGH
(Sgd) E. S. DULIN
Directors

Plaintiff's Exhibit No. 1—(Continued)

CALL AND WAIVER OF NOTICE OF SPECIAL MEETING OF BOARD OF DIRECTORS OF PATTERSON-BALLAGH CORPORATION, Ltd.

We, the undersigned, being all of the Directors of Patterson-Ballagh Corporation, Ltd., desiring to hold a special meeting of the Board of Directors of said corporation, hereby give our written consent to the holding of a special meeting of the said Board for November 2, 1937 at 11:00 o'clock a. m. of the said date, in the offices of Byron Jackson Co., at 2150 East Slauson Avenue, Los Angeles, California, for the purpose of transacting such business as may come before the meeting, and we hereby waive all notice of such meeting and consent to the holding thereof.

And we do further agree that any and all business transacted at said meeting shall be as valid and legal and of the same force and effect as though said meeting were held after notice otherwise duly given, served and published, and we hereby waive notice and publication of notice of the time and place of such meeting of the Board of Directors of said Corporation.

Plaintiff's Exhibit No. 1—(Continued)

Witness our hand this second day of November, 1937.

(Sgd) J. C. BALLAGH
J. C. Ballagh

(Sgd) E. S. DULIN
E. S. Dulin

(Sgd) C. L. PATTERSON
C. L. Patterson
Directors

MINUTES OF SPECIAL MEETING OF BOARD OF DIRECTORS OF PATTERSON-BALLAGH CORPORATION, Ltd.

A special meeting of the Board of Directors of Patterson-Ballagh Corporation, Ltd. was held on the 2nd day of November, 1937, at 11:00 o'clock a. m., in the offices of Byron Jackson Co., at 2150 East Slauson Avenue, Los Angeles, California, there being present and acting at said meeting

J. C. Ballagh
E. S. Dulin
C. L. Patterson

being all of the directors of said corporation.

The meeting was called to order by Mr. C. L. Patterson, who acted as Chairman.

The minutes of the last meeting were read and approved on motion duly made, seconded and unanimously carried.

The Secretary then presented to the meeting the original waiver of notice and consent to the meet-

Plaintiff's Exhibit No. 1—(Continued)

ing, signed by all of the directors, which waiver of notice was, upon motion duly made and carried, ordered to be made a part of the records of this meeting and entered in the Minute Book on the page immediately preceding the minutes of this meeting.

There was a general discussion regarding sales policy in California, and consideration of the bonus, and it was agreed to hold both subjects in abeyance until a later meeting.

In regard to the sales policy in California, it was suggested by Mr. Dulin that the matter of contacting the trade in California be discussed with Medearis to see if the matter could not be handled in a manner more satisfactory to Patterson and Ballagh.

There being no further business to come before the meeting, on motion duly made, seconded and carried, it was thereupon adjourned.

(Sgd) C. L. PATTERSON
C. L. Patterson
Chairman

(Sgd) J. C. BALLAGH
J. C. Ballagh
Secretary

(Sgd) C. L. PATTERSON
(Sgd) J. C. BALLAGH
(Sgd) E. S. DULIN
Directors

Plaintiff's Exhibit No. 1—(Continued)

CALL AND WAIVER OF NOTICE OF SPECIAL MEETING OF BOARD OF DIRECTORS OF PATTERSON-BALLAGH CORPORATION, Ltd.

We, the undersigned, being all of the Directors of Patterson-Ballagh Corporation, Ltd., desiring to hold a special meeting of the Board of Directors of said corporation, hereby give our written consent to the holding of a special meeting of the said Board for December 16, 1937, at 10:30 o'clock a. m. of the said date, in the offices of Byron Jackson Co., at 2150 East Slauson Avenue, Los Angeles, California, for the purpose of transacting such business as may come before the meeting, and we hereby waive all notice of such meeting and consent to the holding thereof.

And we do further agree that any and all business transacted at said meeting shall be as valid and legal and of the same force and effect as though said meeting were held after notice otherwise duly given, served and published, and we hereby waive notice and publication of notice of the time and place of such meeting of the Board of Directors of said corporation.

Plaintiff's Exhibit No. 1—(Continued)

Witness our hand this sixteenth day of December, 1937.

(Sgd) J. C. BALLAGH
J. C. Ballagh

(Sgd) E. S. DULIN
E. S. Dulin

(Sgd) C. L. PATTERSON
C. L. Patterson
Directors

MINUTES OF SPECIAL MEETING OF BOARD OF DIRECTORS OF PATTERSON-BALLAGH CORPORATION, Ltd.

A special meeting of the Board of Directors of Patterson-Ballagh Corporation, Ltd. was held on the 16th day of December, 1937, at 10:30 o'clock a. m. in the offices of Byron Jackson Co., at 1250 East Slauson Avenue, Los Angeles, California, there being present and acting at said meeting

J. C. Ballagh
E. S. Dulin
C. L. Patterson

being all of the directors of said corporation.

The meeting was called to order by Mr. C. L. Patterson who acted as Chairman.

The minutes of the last meeting were read and approved on motion duly made, seconded and unanimously carried.

Plaintiff's Exhibit No. 1—(Continued)

The Secretary then presented to the meeting the original waiver of notice and consent to the meeting, signed by all of the directors, which waiver of notice was, upon motion duly made and carried, ordered to be made a part of the records of this meeting and entered in the Minute Book on the page immediately preceding the minutes of this meeting.

A discussion was had regarding the various tax plans and methods of computation, based on the estimated earnings of the corporation for the year 1937.

No action was taken in regard to the payment of dividends and it was suggested by Mr. Dulin that this matter be held in abeyance until a meeting to be held in February, 1938.

The subject of the payment of bonuses to employees was discussed at length and upon motion duly made and seconded, it was unanimously

> Resolved, That a bonus in a sum not to exceed $2,000.00 be paid the employes of Patterson-Ballagh Corporation in accordance with a plan to be worked out and approved by the officers of the corporation.

The matter of licensing the Bettis Rubber Company under the expander patent owned by Patterson,-Ballagh Corporation was discussed at length and upon motion duly made and seconded, it was unanimously

> Resolved, That Patterson-Ballagh Corporation enter into a license agreement with Bettis

Plaintiff's Exhibit No. 1—(Continued)

Rubber Company on terms approved by Mr. Leonard Lyon of the firm of Lyon & Lyon.

A brief discussion was had relative to the sale of Patterson-Ballagh products in California under the contract held by the California Bettis Company and at the suggestion of Mr. Dulin it was decided to take no action in this matter until it could be discussed with Mr. Ballagh in further detail.

There being no further business to come before the meeting, on motion duly made, seconded and carried, it was thereupon adjourned.

(Sgd) C. L. PATTERSON
Chairman

(Sgd) J. C. BALLAGH
Secretary

CALL AND WAIVER OF NOTICE OF SPECIAL MEETING OF BOARD OF DIRECTORS OF PATTERSON-BALLAGH CORPORATION, Ltd.

We, the undersigned, being all of the Directors of Patterson-Ballgh Corporation, Ltd., desiring to hold a special meeting of the Board of Directors of said corporation, hereby give our written consent to the holding of a special meeting of the said Board for March 11, 1938, at 8:00 o'clock a.m. of said date, in the offices of Byron Jackson Co., at 2150 East Slauson Avenue, Los Angeles, California,

Plaintiff's Exhibit No. 1—(Continued)

for the purpose of discussing such matters as may come before the meeting.

And we do further agree that any and all business transacted at said meeting shall be as valid and legal and of the same force and effect as though said meeting were held after notice otherwise duly given, served and published, and we hereby waive notice and publication of notice of the time and place of such meeting of the Board of Directors of said corporation.

Witness our hands this 11th day of March, 1938.

(Sgd) C. L. PATTERSON
C. L. Patterson

(Sgd) J. C. BALLAGH
J. C. Ballagh

(Sgd) E. S. DULIN.
E. S. Dulin
Directors

CALL AND WAIVER OF NOTICE OF SPECIAL MEETING OF STOCKHOLDERS OF PATTERSON BALLAGH CORPORATION, Ltd.

We, the undersigned, being all of the stockholders of Patterson-Ballagh Corporation, Ltd., desiring to hold a special meeting of the stockholders of said corporation, hereby give our written consent

Plaintiff's Exhibit No. 1—(Continued)

to the holding of a special meeting of the said stockholders for March 11, 1938, at 8:00 o'clock a.m. of the said date, in the offices of Byron Jackson Co., at 2150 East Saulson Avenue, Los Angeles, California, for the purpose of discussing such matters as may come before the meeting.

And we do further agree that any and all business transacted at said meeting shall be as valid and legal and of the same force and effect as though said meeting were held after notice otherwise duly given, served and published, and we hereby waive notice and publication of notice of the time and place of such meeting of the stockholders of said corporation.

Witness our hands this 11th day of March, 1938.

(Sgd) C. L. PATTERSON
C. L. Patterson

(Sgd) J. C. BALLAGH
J. C. Ballagh

(Sgd) E. S. DULIN

BYRON JACKSON CO.
(A corporation by E. S. Dulin, President)

(Sgd) J. C. BALLAGH
Highland Investment Corp., Ltd.
(By J. C. Ballagh, President)

(Sgd) E. S. DULIN
E. S. Dulin
Stockholders

Plaintiff's Exhibit No. 1—(Continued)

MINUTES OF ANNUAL MEETING OF STOCKHOLDERS OF PATTERSON-BALLAGH CORPORATION, Ltd.

The annual meeting of the stockholders of Patterson-Ballagh Corporation, Ltd. was held in the offices of Byron Jackson Co., 2150 East Slauson Avenue, Los Angeles, California, on March 11, 1938, at 8:00 o'clock a.m.

The meeting was called to order by President C. L. Patterson, who acted as Chairman of the meeting, and Mr. J. C. Ballagh acted as Secretary.

Secretary J. C. Ballagh presented to the meeting the original waiver of notice and consent to the meeting, signed by all of the stockholders, which waiver of notice was, upon motion duly made and carried, ordered to be made a part of the records of this meeting and entered in the Minute Book on the page immediately preceding the minutes of this meeting.

The Secretary thereupon called the roll of stockholders and the following report was made of stockholders and stock representatives at the meeting:

Name	No. of shares
Ballagh, J. C.	125
Byron Jackson Co., (a corporation) by E. S. Dulin, Pres.	249
Dulin, E. S.	1
Highland Investment Corp., Ltd. by J. C. Ballagh, Pres.	250
Patterson, C. L.	375
Total Capital Stock	1,000

Plaintiff's Exhibit No. 1—(Continued)

The Secretary reported that the above number of shares represented all of the issued and outstanding stock as of said date.

The financial report of the corporation for the period ending December 31, 1937, as prepared under the direction of the Secretary-Treasurer, was presented and unanimously approved and a summary of same was ordered attached hereto and made a part of the minutes of this meeting.

The Chairman announced that the next business before the meeting was the election of a Board of Directors for the ensuing year. Thereupon, the following were duly nominated as directors to serve until the next annual election and until the election and qualification of their respective successors:

Ballagh, J. C.
Dulin, E. S.
Patterson, C. L.

There being no further business to come before the meeting, on motion duly made, seconded and carried, it was thereupon adjourned.

(Sgd) J. C. BALLAGH
Secretary

(Sgd) C. L. PATTERSON
Chairman

Plaintiff's Exhibit No. 1—(Continued)

Secretary's Report of 1937 Operations

INCOME and PROFIT and LOSS

Gross Sales		$251,049.01
Cost of Goods Sold		68,475.78
		182,573.23
Operating Expenses		157,645.25
Net Operating Profit		24,927.98
Other Expenses—Less Other Income		5,776.01
Net Gain for period, before Income Tax Deduction		19,151.97
Income Tax—1937		4,956.50
Net Gain		14,195.47

Summary of Surplus

Balance as per Ledger 12/31/36		89,326.27
1937 Credits:		
Net Profit from Operations		19,151.97
		108,478.24
1937 Charges:		
Federal Income & Excess Profit Tax 1936	2,618.03	
Correction on Capital Stock Tax	10.00	
Adjustment of Installation Equipment	124.34	
Adjustment of Reserve for Depreciation (Installation Equipment)	135.41	
Federal Income & Excess Profit Tax 1937	4,956.50	7,844.28
Total Earned Surplus		100,633.96
Appreciated Surplus		1,611.86
Total Surplus		$102,245.82

I, J. C. Ballagh, as Secretary-Treasurer of Patterson-Ballagh Corporation, Ltd., hereby certify that the foregoing report is true, to the best of my knowledge and belief.

(Sgd) J. C. BALLAGH

Plaintiff's Exhibit No. 1—(Continued)

MINUTES OF ANNUAL MEETING OF DIRECTORS OF PATTERSON-BALLAGH CORPORATION, Ltd.

The annual meeting of directors of Patterson-Ballagh Corporation, Ltd. was held in the offices of Byron Jackson Co., 2150 East Slauson Avenue, Los Angeles, California, on March 11, 1938, immediately following the annual meeting of the stockholders.

There were present and acting at said meeting

J. C. Ballagh
E. S. Dulin
C. L. Patterson

being all of the directors of said corporation.

The meeting was called to order by Mr. C. L. Patterson, who acted as Chairman of the meeting, and Mr. J. C. Ballagh acted as Secretary.

Secretary J. C. Ballagh presented to the meeting the original waiver of notice and consent to the meeting, signed by all of the stockholders, which waiver of notice was, upon motion duly made and carried, ordered to be made a part of the records of this meeting and entered in the Minute Book on the page immediately preceding the minutes of this meeting.

The Chairman stated that the first business to come before the meeting was the election of officers for the ensuing year, and the following persons were nominated for the ensuing year for the respective offices, to-wit:

C. L. Patterson—President
J. C. Ballagh—Secretary-Treasurer

Plaintiff's Exhibit No. 1—(Continued)

There being no further nominations, and the nominations of the above named persons being duly seconded, a vote was had and the Secretary declared the said persons unanimously nominated for the said respective offices for the ensuing year.

There being no further business to come before the meeting, on motion duly made, seconded and carried, it was thereupon adjourned.

(Sgd) C. L. PATTERSON
Chairman

(Sgd) J. C. BALLAGH
Secretary

(Sgd) J. C. BALLAGH
J. C. Ballagh

E. S. Dulin
(Sgd) C. L. PATTERSON
C. L. Patterson
Directors

MINUTES OF SPECIAL MEETING OF BOARD OF DIRECTORS OF PATTERSON-BALLAGH CORPORATION, Ltd.

A special meeting of the Board of Directors of Patterson-Ballagh Corporation, Ltd. was held on the 11th day of March, 1938, immediately following the Annual Meeting of Directors, in the offices of Byron Jackson Co., 2150 East Slauson Avenue, Los Angeles, California, there being present and acting at said meeting

Plaintiff's Exhibit No. 1—(Continued)

C. J. Ballagh

E. S. Dulin

C. L. Patterson

being all of the directors of said corporation.

The meeting was called to order by Mr. C. L. Patterson, who acted as Chairman of the meeting, and Mr. J. C. Ballagh acted as Secretary.

Secretary J. C. Ballagh presented to the meeting the original waiver of notice and consent to the meeting, signed by all of the directors, which waiver of notice was, upon motion duly made and carried, ordered to be made a part of the records of this meeting and entered in the Minute Book on the page immediately preceding the minutes of this meeting.

There was a general discussion relative to the financial statements during which it was brought out that these statements did not show the gain before tax, with an estimate of what the taxes would be, and the net after the tax. It was suggested by Mr. Dulin that these reports when issued show the gain in the manner outlined above and that this same information be shown on the auditor's report.

The matter of patent infringement was discussed, and upon motion duly made, seconded and carried, it was unanimously

Resolved, That Patterson-Ballagh Corporation, Ltd. proceed with the suit against the Rubber Sleeve Specialty Company for alleged infringement in Arkansas, the suit to be filed

Plaintiff's Exhibit No. 1—(Continued)

subject to approval of Leonard Lyon and carried forward in a manner subject to his approval.

The next matter for discussion was the recommendation of Mr. W. W. Cahoon for salary increases for the various employees in the Accounting Department. After a general discussion it was unanimously decided that the increases as recommended be not made at this time and the suggestion made that the matter be brought before the Board again within the next month or two.

A letter from Mr. J. M. O'Melveny, Mid-Continent Sales Manager, was presented to the Board by the Secretary, recommending a blanket increase in salary of ten dollars per month for the various sales and field men in the Mid-Continent.

After a general discussion as to business prospects, both in the oil industry and business in general, it was moved by Mr. Dulin and seconded by Mr. Patterson that no blanket increases in salaries be made at this time. Mr. Ballagh made a motion to the contrary, stating that, in his opinion, Mr. O'Melveny was in a better position to make recommendations along this line and, therefore, believed that Mr. O'Melveny's recommendation should be accepted.

It was unanimously agreed that Mr. Ballagh should write Mr. O'Melveny, explaining the stand taken by the Board in regard to blanket increases, and obtain from him a recommendation to spot increases in salaries of the men to bring the salaries

Plaintiff's Exhibit No. 1—(Continued)

up to levels comparable with those paid by other oil tool companies.

The matter of appointing a new resident agent in Louisiana was discussed and upon motion duly made and seconded, it was unanimously.

> Resolved, That Mr. R. C. Medearis of New Iberia, Louisiana, be appointed Resident Agent in Louisiana to succeed Mr. Fred. Bennett.

The matter of licensing the Bettis Rubber Company under the expander patent, owned by Patterson-Ballagh Corporation, came up for further discussion and upon motion duly made and seconded it was unanimously

> Resolved, That the Resolution adopted at the meeting held December 16, 1937, authorizing a license agreement with Bettis Rubber Company, be herewith nullified.

There being no further business to come before the meeting, on motion duly made, seconded and carried, it was thereupon adjourned.

(Sgd) C. L. PATTERSON
Chariman

(Sgd) J. C. BALLAGH
Secretary

(Sgd) C. L. PATTERSON

(Sgd) E. S. DULIN

(Sgd) J. C. BALLAGH
Directors

Plaintiff's Exhibit No. 1—(Continued)

CALL AND WAIVER OF NOTICE OF SPECIAL MEETING OF BOARD OF DIRECTORS OF PATTERSON-BALLAGH CORPORATION, Ltd.

We, the undersigned, being all of the Directors of Patterson-Ballagh Corporation, Ltd., desiring to hold a special meeting of the Board of Directors of said corporation, hereby give our written consent to the holding of a special meeting of the said board for March 24, 1938, at 11:00 o'clock a.m. of said date, in the offices of Byron Jackson Co., at 2150 East Slauson Avenue, Los Angeles, California, for the purpose of discussing such matters as may come before the meeting.

And we do further agree that any and all business transacted at said meeting shall be as valid and legal and of the same force and effect as though said meeting were held after notice otherwise duly given, served and published, and we hereby waive notice and publication of notice of the time and place of such meeting of the Board of Directors of said corporation.

Witness our hands this 24th day of March, 1938.

(Sgd) C. L. PATTERSON
C. L. Patterson

(Sgd) J. C. BALLAGH
J. C. Ballagh

E. S. Dulin
Directors

Plaintiff's Exhibit No. 1—(Continued)

MINUTES OF SPECIAL MEETING OF BOARD OF DIRECTORS OF PATTERSON-BALLAGH CORPORATION, Ltd.

A special meeting of the Board of Directors of Patterson-Ballagh Corporation, Ltd. was held on the 24th day of March, 1938, at 11:00 o'clock a.m. in the offices of Byron Jackson Co., at 1250 East Slauson Avenue, Los Angeles, California, there being present and acting at said meeting

J. C. Ballagh
E. S. Dulin
C. L. Patterson

being all of the directors of said corporation.

The meeting was called to order by Mr. C. L. Patterson, who acted as Chairman of the meeting, and Mr. J. C. Ballagh acted as Secretary.

Secretary J. C. Ballagh presented to the meeting the original waiver of notice and consent to the meeting, signed by all of the directors, which waiver of notice was, upon motion duly made and carried, ordered to be made a part of the records of this meeting and entered in the Minute Book on the page immediately preceding the minutes of this meeting.

The Secretary reported that a letter had been received from Mr. O'Melveny, in answer to the letter written him advising the stand taken by the Board in regard to blanket increases in salaries, recommending increases for three of the men in the Mid-Continent, and upon motion duly made and seconded it was unanimously

Plaintiff's Exhibit No. 1—(Continued)

Resolved, That the salaries of R. C. Medearis, W. B. Gardner and Ray Morris be increased Ten Dollars per month, effective March 15, 1938.

The matter of increases in salaries for employees in the Accounting Department, as recommended by Mr. W. W. Cahoon at the previous meeting, came up for further discussion, and it was moved, seconded and unanimously

Resolved, that the salaries of W. S. Sharp, Fred. Bollinger and C. Carpenter be increased as follows, effective March 15, 1938:

Sharp ----------$8.00 per month
Bollinger ------- 7.50 " "
Carpenter ------- 5.00 " "

There being no further business to come before the meeting, on motion duly made, seconded and carried, it was thereupon adjourned.

(Sgd) C. L. PATTERSON
Chairman

(Sgd) J. C. BALLAGH
Secretary

(Sgd) C. L. PATTERSON

(Sgd) E. S. DULIN

(Sgd) J. C. BALLAGH
Directors

Plaintiff's Exhibit No. 1—(Continued)

MINUTES OF SPECIAL MEETING OF BOARD OF DIRECTORS OF PATTERSON-BALLAGH CORPORATION, Ltd.

A special meeting of the Board of Directors of Patterson-Ballagh Corporation, Ltd. was held on the 29th day of April, 1938, at 10:00 o'clock a.m. in the offices of the corporation at 1900 East 65th Street, Los Angeles, California, pursuant to notice issued.

There were present and acting at said meeting

J. C. Ballagh

C. L. Patterson

Director E. S. Dulin was absent.

The meeting was called to order by Mr. C. L. Patterson who acted as Chairman.

The minutes of the last meeting were read and approved on motion duly made, seconded and unanimously carried.

The Chairman announced that the first thing to come before the meeting was the matter of transferring the bank account carried with the South Texas Commercial National Bank in Houston, Texas, from the name of J. M. O'Melveny to Patterson-Ballagh Corporation, Ltd.

Upon motion duly made and seconded it was unanimously

Resolved, That the account with the South Texas Commercial National Bank in Houston, Texas, formerly carried in the name of J. M. O'Melveny be transferred to Patterson-Ballagh

Plaintiff's Exhibit No. 1—(Continued)

Corporation, Ltd., and that checks against this account be signed by J. M. O'Melveny as District Manager;

Resolved Further, That arrangements be made with the bank so that funds may be withdrawn from this account on the signature of C. L. Patterson, J. C. Ballagh or J. M. O'Melveny.

There being no further business to come before the meeting, on motion duly made, seconded and carried, it was thereupon adjourned.

(Sgd) C. L. PATTERSON
President.

(Sgd) J. C. BALLAGH
Secretary

(Sgd) J. C. BALLAGH
J. C. Ballagh

(Sgd) C. L. PATTERSON
C. L. Patterson
Directors

CALL AND WAIVER OF NOTICE OF SPECIAL MEETING OF BOARD OF DIRECTORS OF PATTERSON-BALLAGH CORPORATION, Ltd.

We, the undersigned, being all of the Directors of Patterson-Ballagh Corporation, Ltd., desiring to hold a special meeting of the Board of Directors

Plaintiff's Exhibit No. 1—(Continued)

of said corporation, hereby give our written consent to the holding of a special meeting of the said board for June 20, 1938, at 3:00 o'clock p.m. of said date, in the offices of Byron Jackson Co., at 2150 East Slauson Avenue, Los Angeles, California, for the purpose of discussing such matters as may come before the meeting.

And we do further agree that any and all business transacted at said meeting shall be as valid and legal and of the same force and effect as though said meeting were held after notice otherwise duly given, served and published, and we hereby waive notice and publication of notice of the time and place of such meeting of the Board of Directors of said corporation.

Witness our hands this 20th day of June, 1938.

(Sgd) C. L. PATTERSON
C. L. Patterson

(Sgd) J. C. BALLAGH

(Sgd) E. S. DULIN
E. S. Dulin
Directors

MINUTES OF SPECIAL MEETING OF BOARD OF DIRECTORS OF PATTERSON-BALLAGH CORPORATION, Ltd.

A special meeting of the Board of Directors of Patterson-Ballagh Corporation, Ltd. was held on

Plaintiff's Exhibit No. 1—(Continued)

the 20th day of June, 1938, at 3:00 o'clock p.m. in the offices of Byron Jackson Co., at 1250 East Slauson Avenue, Los Angeles, California, there being present and acting at said meeting

J. C. Ballagh
E. S. Dulin
C. L. Patterson

being all of the directors of said corporation.

The meeting was called to order by Mr. C. L. Patterson, who acted as Chairman of the meeting, and Mr. J. C. Ballagh acted as Secretary.

Secretary J. C. Ballagh presented to the meeting the original waiver of notice and consent to the meeting, signed by all of the directors, which waiver of notice was, upon motion duly made and carried, ordered to be made a part of the records of this meeting and entered in the Minute Book on the page immediately preceding the minutes of this meeting.

The Secretary presented to the Board a letter received from Mr. J. M. O'Melveny, of Houston, Texas, requesting an increase in salary and a bonus, together with a recommendation for an increase in salary for Mr. T. M. Smith, Jr.

After a general discussion, and upon motion duly made and seconded it was unanimously

Resolved, That the salary of Mr. J. M. O'Melveny be increased from $354.00 to $375.00, effective July 1, 1938;

Resolved Further, That Mr. O'Melveny be

Plaintiff's Exhibit No. 1—(Continued)

given a bonus of $25.00 when sales in the Mid-Continent area (comprising the states of Texas, Louisiana, Oklahoma, Arkansas, New Mexico and Illinois) exceed $15,000.00 in any one month; $50.00 when the sales exceed $18,000.00 and $75.00 when the sales exceed $21,000.00. This will in no way affect any yearly bonus which may be paid by the corporation;

Resolved Further, That the salary of Mr. T. M. Smith, Jr. be increased from $160.00 to $170.00 per month, effective July 1, 1938;

Resolved Further, That a dividend of six (6) per cent of the capital stock be paid out of the profits of the corporation, earned prior to June 30, 1938, to the stockholders on record as of June 30, 1938.

There being no further business to come before the meeting, on motion duly made, seconded and carried, it was thereupon adjourned.

(Sgd) C. L. PATTERSON
Chairman

(Sgd) J. C. BALLAGH
Secretary

(Sgd) C. L. PATTERSON

(Sgd) J. C. BALLAGH
Directors

Plaintiff's Exhibit No. 1—(Continued)

WRITTEN ASSENT OF SHAREHOLDERS TO AMENDMENT OF BY-LAWS OF PATTERSON-BALLAGH CORPORATION, Ltd.

Know All Men by These Presents:

That we, the undersigned, being the holders of subscribed shares entitled to exercise a majority of the voting power of Patterson-Ballagh Corporation, a California corporation, and each holding the number of such shares hereinbelow indicated after the name of each, do hereby assent to the adoption of, and amendments to, the By-Laws of said corporation as follows:

Section 1, Article I.

"The annual meetings of the stockholders shall be held on the first Tuesday following the 10th of January in each year, at 8:30 o'clock A.M.*

Section 1, Article II. Powers

"Subject to limitations of the articles of incorporation, of the by-laws, and of title one of part four of division first of the California Civil Code as to action to be authorized or approved by the shareholders, and subject to the duties of directors as prescribed by the by-laws, all corporate powers shall be exercised by or under the authority of, and the business and affairs of the corporation shall be controlled by, the board of directors.*

Plaintiff's Exhibit No. 1—(Continued)

Section 2, Article II Number and Qualification.

"The authorized number of directors of the corporation shall be five until changed by amendment of the articles of incorporation or by a by-law amending this Section 2 of Article II of these by-laws duly adopted by the vote or written assents of the shareholders entitled to exercise a majority of the voting power of the corporation."

Section 5, Article II Place of Business.

"The principal place of business and office of the corporation shall be 1900 East 65th Street, Los Angeles, California, until the Board of Directors shall otherwise provide."

Section 6, Article II. Meetings.

"Regular meetings of the Board of Directors shall be held at the principal place of business, or office of the corporation, on the first Tuesday following the 10th of each month at 8:30 o'clock A.M. It shall not be necessary to give notice of any of such meetings nor of the business to be transacted. Special meetings of said Board may be called upon the order of the President, or any two directors; and the Secretary shall give three days' notice in writing, by mail, of the meeting to each director; provided, that a meeting may be held at any time without notice if all the directors are present or consent thereto in writing or by telegram; and a meeting of the directors may be held

Plaintiff's Exhibit No. 1—(Continued)

without notice immediately after the annual meeting; provided, further, that the first regular meeting of said Board for the transaction of any and all business shall be held at the said office of the corporation immediately after the adoption of these By-Laws."

Article VIII. Amendments.

"Section 1. Power of Shareholders. New By-Laws may be adopted or these by-laws may be amended or repealed by the vote of shareholders entitled to exercise a majority of the voting power of the corporation or by the written assent of such shareholders.

Section 2. Power of Directors. Subject to the right of shareholders as provided in Section 1 of this Article VIII to adopt, amend or repeal by-laws, by-laws other than a by-law or amendment thereof changing the authorized number of directors may be adopted, amended or repealed by the board of directors".

and we hereby adopt the same as and for By-Laws of said corporation.

In Witness Whereof we have hereunto subscribed our names this 4th day of August, 1938.

Name	No. of Shares
Highland Investment Corp.	375
.....	
By (Sgd) J. C. Ballagh	
(Sgd) C. L. Patterson	375
.....	.....

Plaintiff's Exhibit No. 1—(Continued)

MINUTES OF MEETING OF BOARD OF DIRECTORS OF PATTERSON-BALLAGH CORPORATION, LTD.

A meeting of the Board of Directors of Patterson-Ballagh Corporation, Ltd., was held August 6, 1938, at the hour of 11:00 o'clock, A. M., at the office of the Company, 1900 East 65th Street, Los Angeles, California, pursuant to notice regularly served on each Director as provided in the By-Laws.

Those present were:

J. C. Ballagh,
C. L. Patterson,
E. S. Dulin,

constituting all of the members of the Board.

The President called the meeting to order and stated that the first order of business was the reading of the minutes of the previous meeting of the Board.

Upon motion duly made, seconded and carried the reading of the minutes of the previous meeting of the Board was dispensed with.

The President announced that the By-Laws had been amended by the stockholders as provided by law, and that they now provided for five directors instead of three as formerly. He stated that it was now in order to add two directors to the Board. Whereupon, on motion duly made and seconded and unanimously carried, J. C. Rennie and H. W. Elliott were elected directors. Mr. Rennie and Mr.

Plaintiff's Exhibit No. 1—(Continued)

Elliott being present, accepted the directorship and thereafter participated in the meeting.

The next matter of business was the question of bonding employees of the company who handle money or property of the company. After a general discussion the following resolution was moved by Mr. Dulin, seconded by Mr. Elliott:

> Resolved: That all employees of the corporation who handle money, or in whose possession any of the property of the company is placed, or who may draw checks on any of the company's funds, shall be bonded by a fidelity bond in a company, and to an amount satisfactory to the Board.

On vote the resolution was unanimously adopted.

The next order of business was the matter of the collection of accounts in Texas and other mid-continent areas, and the disposition of such collections. After a general discussion the following resolution was moved by Mr. Dulin, seconded by Mr. Elliott:

> Resolved: That all collections of accounts in Texas and other mid-continent areas should be forwarded to the principal office of the company in Los Angeles for deposit and that all deposits made in the Houston account shall be made by check from the home office in Los Angeles.

On vote the resolution was unanimously adopted.

The next order of business was the question of advances to employees. The following resolution was moved by Mr. Dulin, seconded by Mr. Elliott:

Plaintiff's Exhibit No. 1—(Continued)

Resolved: That all advances to employees other than those having to do with a revolving expense account, shall be subject to the approval of the Board of Directors.

On vote being taken it was unanimously carried.

The next matter of business was the question of experimental work being carried on and the cost thereof. After a general discussion the following resolution was moved by Mr. Dulin, seconded by Mr. Elliott:

Resolved: That a monthly report to the Board be made by the experimental department covering the number of items under experimentation, a general statement of the progress being made, and a statement of the amount of money being expended on each item.

On vote, the resolution was unanimously adopted.

At this point, Mr. Dulin retired from the meeting, but the Board continued in session.

The next matter of business was the question of the payment of a director's fee for attendance upon Director's meetings. After a general discussion, the following resolution was moved by Mr. Patterson, seconded by Mr. Ballagh:

Resolved: That a fee of $20.00 shall be paid to each director who is not a stockholder, attending a meeting of the Board at both regular and special meetings.

On vote, the resolution was unanimously adopted.

There being no further business to come before

Plaintiff's Exhibit No. 1—(Continued)

the meeting, on motion duly made, seconded and carried, the meeting adjourned.

(Sgd) J. C. BALLAGH,
Secretary.

Attest:

(Sgd) C. L. PATTERSON,
President.

MINUTES OF SPECIAL MEETING OF BOARD OF DIRECTORS OF PATTERSON-BALLAGH CORPORATION, LTD.

A special meeting of the Board of Directors of Patterson-Ballagh Corporation, Ltd., was held at the office of the company, 1900 East 65th Street, Los Angeles, California, at the hour of 8:30 A.M., on September 27, 1938, pursuant to notice served on each of the directors at the time and in the manner required by the By-Laws.

Present:

C. L. Patterson
J. C. Ballagh
J. C. Rennie
H. W. Elliott

Absent:

E. S. Dulin

Mr. W. H. Weise was present at the meeting by invitation as an observer for Byron Jackson Co.

Plaintiff's Exhibit No. 1—(Continued)

The President declared a quorum present and called the meeting to order.

The minutes of the preceding meeting were read and it was moved by Mr. Elliott, seconded by Mr. Rennie, that said minutes be approved as read. Motion unanimously carried.

On the unfinished business, the President reported that application had been made for a blanket bond on all employees, and that the same was now in effect. He stated that this blanket bond was in lieu of the bond covering individuals mentioned in the resolution of the last meeting. The President explained that the blanket bond was simpler than the bond covering specific individuals because the individual applications would have to be filed. It was moved by Mr. Rennie, seconded by Mr. Ballagh, that the blanket bond be approved in the place of the bond covering specific individuals. Motion unanimously carried.

The President reported that the bank at Houston would be notified at once relative to acceptance of deposits only from Los Angeles.

On the matter of advances to officers and employees, the President explained that $388.85 had been advanced to Mr. J. M. O'Melveny at the time of sickness, and that this sum was covered by a note to the corporation and repayment arranged on a monthly basis. It was moved by Mr. Rennie, seconded by Mr. Elliott, that this arrangement be approved. Motion unanimously carried.

Plaintiff's Exhibit No. 1—(Continued)

The President reported on experimental work and the cost thereof substantially as follows:

1.—Mixing bowl, $445.81. Dormant at the present time.

2.—Expander Safety Screen. $18.19. Now on production.

3.—Cat Line Roller, $79.38. This was a model only, made to the specifications of J. C. Ballagh. Mr. Ballagh reports that this project is now dormant as the model is not of enough interest to the oil companies to justify production, and that in his opinion it would not be approved enough by customers to justify its manufacture.

4.—Derrick Window Roller, $183.22. This was made on the design of J. C. B. and the first one as made is now on a derrick of the Union Oil Company for test and until the tests are completed no further production will be made.

5.—Experimental Laboratory, $517.56. Mr. Patterson reported that the laboratory is for experiments being carried on.

6.—Experimental work on materials and molds —especially plastics, $252.53. These experimentals are being continued.

7.—Miscellaneous, $463.61. This item includes tubing protector, sucker rod protector and cost of experimental material used in connection therewith. The tubing protector has been o.k.'d as to design and is now on production. On the sucker rod protector this item is still in the experimental stage.

Plaintiff's Exhibit No. 1—(Continued)

8.—Coated Pony Rod. Mr. Patterson reported that the $10.00 spent on this item to date is included in the miscellaneous item under No. 7. This is still in the experimental stage.

It was moved by Mr. Elliott, seconded by Mr. Rennie, that the President's report of experimental work and the cost thereof, be approved. Motion unanimously carried.

In the matter of general insurance, the President stated that he had obtained two reports, one from Nettleship and one from Maloney, on insurance matters, and stated that the coverage which was previously lacking had been obtained. It was moved by Mr. Rennie, seconded by Mr. Elliott, that the President's report be accepted and approved. Motion unanimously carried.

The next question was the matter of setting aside monthly reserves to cover the estimated income tax payments. It was moved by Mr. Elliott, seconded by Mr. Rennie, that cash equal to the book reserve be deposited in the fund account at the Security-First National Bank to cover the estimated income tax liability on monthly earnings. Motion unanimously carried.

The next matter was the consideration of the salaries of officers. The Secretary reported that a wire had been received from Mr. Dulin requesting that action on this matter be deferred until he could be present, stating his inability to be present at this time. Mr. Elliott likewise stated that inasmuch as he was a new member of the Board, he

Plaintiff's Exhibit No. 1—(Continued)

would like an opportunity to familiarize himself further with the financial condition of the company, its earnings for the current year, and its dividend records of the past. No action was taken on the matter of officers' salaries.

On the matter of employees' salaries, it was moved by Mr. Ballagh, seconded by Mr. Rennie, that the salary of J. M. O'Melveny be raised from $375.00 to $450.00 per month, effective October 1, 1938. Motion unanimously carried.

It was moved by Mr. Ballagh, seconded by Mr. Rennie, that the salary of Mr. R. A. McWaid be increased from $375.00 to $400.00 per month, effective October 1, 1938. Motion unanimously carried.

Mr. Rennie made a report on the expanding equipment and explained how it was in general use and was scattered and unaccounted for. He suggested that steps be taken to follow more closely the location and tracing of the company's expanding equipment. It was moved by Mr. Elliott, seconded by Mr. Ballagh, that the report be approved. Motion unanimously carried.

The next matter before the Board was the change of the corporation name from Patterson-Ballagh Corporation, Ltd., to Patterson-Ballagh Corporation. After some discussion the following resolution covering an amendment of the Articles of Incorporation to change the corporate name of Patterson-Ballagh Corporation, Ltd., was presented. Upon motion by Mr. Elliott, seconded by Mr. Bal-

Plaintiff's Exhibit No. 1—(Continued)

lagh, and unanimously carried, the following resolution was adopted:

"Whereas, it is deemed by the Board of Directors of this corporation to be to the best interests of its shareholders and all persons interested therein that its Articles of Incorporation be amended for the purpose of eliminating the word "Ltd." from its corporate name,

"Now, Therefore Be It Resolved, that Article First of the Articles of Incorporation of this corporation shall be amended to read as follows:

'First: That the name of this corporation shall be Patterson-Ballagh Corporation.'

"Further Resolved, that the Board of Directors of this corporation hereby adopts and approves the foregoing amendment of its Articles of Incorporation:

"Further Resolved: that the President or Vice-President and the Secretary of this corporation shall be and they are hereby authorized and directed to procure the adoption and approval of the foregoing amendment of its Articles of Incorporation by the vote or written consent of the shareholders of the corporation holding at least a majority of the voting power, and, thereafter, to sign and verify by their oaths and to file a certificate in the form and manner required by Section 362-b of the Civil

Plaintiff's Exhibit No. 1—(Continued)

Code of the State of California, and in general to do any and all things necessary to effect said amendment in accordance with the terms, provisions and requirements of said Section 362-b.*

The next order of business was the consideration of increasing purchases of rubber to cover six months futures. The matter was thoroughly discussed and it was moved by Mr. Ballagh, seconded by Mr. Elliott, that authority be given to the officers to increase the purchase of smoke sheet rubber when and as they may deem it advisable to cover six months future requirements of the Company. Motion unanimously carried.

The next matter of business was the question of the infringement of the company's patents and articles by McGregor Brothers of Long Beach. The Secretary explained that the company had received opinions of patent counsel that infringement was taking place, and that an action was justified. It was moved by Mr. Ballagh, seconded by Mr. Rennie, that authority be granted to start an infringement action against McGregor Brothers of Long Beach. Motion unanimously carried.

The Secretary also reported that it seemed advisable to transfer the suit of Ralph Howard from Louisiana to Oklahoma. It was moved by Mr. Ballagh, seconded by Mr. Rennie, that authority be granted to transfer the suit of Ralph Howard from Louisiana to Oklahoma. Motion unanimously carried.

Plaintiff's Exhibit No. 1—(Continued)

The Secretary then pointed out that the company had been invited to join the Metal Trade Manufacturers Association. A general discussion was had in regard to the matter and it was moved by Mr. Ballagh, seconded by Mr. Elliott, that the company join the Metal Trade Manufacturers Association. On vote the following directors voted in the affirmative: J. C. Ballagh, J. C. Rennie, H. W. Elliott; negative, C. L. Patterson.

The matter of the Fair Labor Standards Act of 1938 was brought up and a general discussion was had. It was moved by Mr. Ballagh, seconded by Mr. Elliott, that the employees of Patterson-Ballagh affected by the Act be employed on the basis of a 40-hour week and time and one-half for overtime, effective October 1, 1938. Motion unanimously carried.

The matter of a sick benefit insurance plan for the employees was brought up for discussion by the President. A general discussion was had and it was moved by Mr. Ballagh, seconded by Mr. Patterson, that the insurance and sick benefit plan that has been presented to the employees for their approval, be approved subject to the approval of the majority of the employees. Motion unanimously carried.

Mr. Ballagh then notified the Board that he was considering a proposed trip to the Trinidad and Venezuela area during the coming Spring, should conditions then be favorable. He stated that he did not wish the Board to take any action on the

Plaintiff's Exhibit No. 1—(Continued)

matter at this time, but merely wanted to notify the Board of his intended trip.

There being no further business to come before the meeting, on motion duly made, seconded and carried, the meeting adjourned.

Attest:

(Sgd) C. L. PATTERSON,
President.

(Sgd) J. C. BALLAGH,
Secretary.

CALL AND WAIVER OF NOTICE OF MEETING OF BOARD OF DIRECTORS OF PATTERSON-BALLAGH CORPORATION

We, the undersigned, being all of the Directors of Patterson-Ballagh Corporation, desiring to hold a meeting of the Board of Directors of said corporation, hereby give our written consent to the holding of a special meeting of the said Board for October 13, 1938, at 8:30 o'clock a.m., of said date, at the office and principal place of business of the company, 1900 East 65th Street, Los Angeles, California.

And we do further agree that any and all business transacted at said meeting shall be as valid and legal and of the same force and effect as though said meeting were held after notice otherwise duly given, served and published, and we hereby waive notice and publication of notice of the time and

Plaintiff's Exhibit No. 1—(Continued)

place of such meeting of the Board of Directors of said corporation.

Witness our hands this 13th day of October, 1938.

(Sgd) C. L. PATTERSON,
(Sgd) J. C. BALLAGH,
(Sgd) J. C. RENNIE,
Directors.

MINUTES OF MEETING OF BOARD OF DIRECTORS OF PATTERSON-BALLAGH CORPORATION

A meeting of the Board of Directors of Patterson-Ballagh Corporation was held at the office and principal place of business of the company, 1900 East 65th Street, Los Angeles, California, on the 13th day of October, 1938, at the hour of 8:30 o'clock A.M., there being present and acting at said meeting

C. L. Patterson
J. C. Ballagh
J. C. Rennie
E. S. Dulin
H. W. Elliott

The President declared a quorum present and called the meeting to order.

The Secretary presented to the meeting the original waiver of notice and consent to the meeting, signed by all of the directors, which waiver of notice was, upon motion duly made and carried, ordered to be made a part of the records of this meeting and

Plaintiff's Exhibit No. 1—(Continued)

entered in the Minute Book on the page immediately preceding the minutes of this meeting.

The first order of business was the reading of the minutes of the preceding meeting of the Board. The minutes were read and it was moved by Mr. Elliott, seconded by Mr. Rennie that the minutes be approved as read. Motion unanimously carried.

The Secretary then pointed out the necessity of appointing a resident agent in Louisiana to succeed Mr. R. C. Medearis. It was moved by Mr. Rennie, seconded by Mr. Ballagh, that Mr.
be appointed as resident agent in Louisiana to succeed R. C. Medearis. Motion unanimously carried.

The next order of business was the consideration of the increase in salaries of employees.

The President recommended an increase in salary of $10.00 per month to W. T. Gardner and $10.00 per month to Ross Mauldin, upon the recommendation of Mid-Continent Sales Manager, J. M. O'Melveny. It was moved by Mr. Rennie, seconded by Mr. Elliott, that the salaries of Mr. Gardner and Mr. Mauldin be each increased $10.00 per month, effective October 1, 1938. Motion unanimously carried.

Mr. Dulin then spoke of the advisability of paying the balance due on the mortgage on the factory property, and thereby clear the company of all indebtedness. After a general discussion it was moved by Mr. Dulin, seconded by Mr. Rennie, that the officers of the corporation ascertain from the Bank upon what basis the present mortgage could be paid and

Plaintiff's Exhibit No. 1—(Continued)

report their findings to the next meeting. Motion unanimously carried.

The next matter before the meeting was the matter of the increase in the officers' salaries. A general discussion was had and it was moved by Mr. Dulin, seconded by Mr. Elliott, that the salary of Mr. C. L. Patterson, President, be increased to $1500.00 per month, effective September 1, 1938. Motion unanimously carried. It was thereupon moved by Mr. Dulin, seconded by Mr. Elliott, that the salary of Mr. J. C. Ballagh, Secretary-Treasurer of the company, be increased to $1500.00 per month, effective September 1, 1938. Motion unanimously carried.

The next question was the matter of a possible advantage to the company by changing the fiscal year to close as of November 30, 1938. A general discussion was had and it was moved by Mr. Dulin, seconded by Mr. Elliott, that the fiscal year of the corporation be fixed to close as of November 30th of each year, subject to approval of our accountants, in place of December 31st, as at present designated. Motion unanimously carried.

There being no further business to come before the meeting, on motion duly made, seconded and carried, the meeting adjourned.

Attest:

(Sgd) J. C. BALLAGH,
Secretary.

(Sgd) C. L. PATTERSON,
President.

Plaintiff's Exhibit No. 1—(Continued)

MINUTES OF MEETING OF BOARD OF DIRECTORS OF PATTERSON-BALLAGH CORPORATION

A meeting of the Board of Directors of Patterson-Ballagh Corporation was held at the office and principal place of business of the company, 1900 East 65th Street, Los Angeles, California, on the 3rd day of November, 1938, at the hour of 8:30 o'clock a.m., pursuant to notice issued.

Present:

J. C. Ballagh
C. L. Patterson
E. S. Dulin
H. W. Elliott
J. C. Rennie

being all of the Directors of said corporation.

The President declared a quorum present and called the meeting to order.

The first order of business was the reading of the minutes of the preceding meeting of the Board. The minutes were read and it was moved by Mr. Elliott, seconded by Mr. Rennie that the minutes be approved as read. Motion unanimously carried.

The next order of business was the matter of the contract with the Medearis Oilwell Supply Company which was terminated October 28, 1938. A general discussion was had and it was moved by Mr. Elliott, seconded by Mr. Dulin, that a letter be sent to Medearis Oilwell Supply Company by special delivery, registered mail, calling attention to the thirty

Plaintiff's Exhibit No. 1—(Continued)

day cancellation clause in the contract. Motion unanimously carried.

It was moved by Mr. Dulin, seconded by Mr. Rennie, that Mr. Elliott render an opinion at the next meeting as to whether the company had cause of action against Medearis Oilwell Supply Company for breach of contract as representative of this company. Motion unanimously carried.

There being insufficient time to discuss the further business scheduled for this meeting, on motion duly made, seconded and carried, the meeting adjourned until Thursday, November 10, 1938, at 8:30 a.m.

Attest:

(Sgd) J. C. BALLAGH,
Secretary.

(Sgd) C. L. PATTERSON,
President.

MINUTES OF SPECIAL MEETING OF BOARD OF DIRECTORS OF PATTERSON-BALLAGH CORPORATION

A special meeting of the Board of Directors of Patterson-Ballagh Corporation was held at the office of the company, 1900 East 65th Street, Los Angeles, California, on the 10th day of November, 1938, at the hour of 8:30 a.m., pursuant to notice issued.

Plaintiff's Exhibit No. 1—(Continued)

Present:

C. L. Patterson
J. C. Ballagh
H. W. Elliott
J. C. Rennie

Absent:

E. S. Dulin

The President declared a quorum present and called the meeting to order.

The minutes of the preceding meeting were read and it was moved by Mr. Elliott, seconded by Mr. Rennie, that said minutes be approved as read. Motion unanimously carried.

On the unfinished business, Mr. Elliott stated that, after making a careful study of the contract and correspondence which has taken place, and facts pertaining to the notice of termination of the contract by Medearis Oilwell Supply Company, it is his opinion there is no cause of action which would justify this company in filing suit against Medearis Oilwell Supply Company. Mr. Elliott recommended that no action be taken at the present time. On motion of Mr. Rennie, seconded by Mr. Ballagh, the recommendation was unanimously accepted.

The officers reported that the bank would be willing to accept payment of the mortgage without any bonus. The President stated, however, in view of the present state of the business in California, particularly the competition that has developed, that the matter of payment of the mortgage be deferred for the present. It was moved by Mr. Elliott, sec-

Plaintiff's Exhibit No. 1—(Continued)

onded by Mr. Rennie, that the President's recommendation be accepted and payment of the mortgage be deferred. Motion unanimously carried.

Mr. Rennie stated that he was not prepared at the present time to make a final report on the matter of the change in the fiscal year to end November 30th, but that before the end of this month (November) he will be able to do so, based upon the financial statement of the company at the close of business as of October 31, 1938, which is not available at this time. It was the concensus of opinion of the Board that another meeting should be held before the close of the month.

The President reported on experimental work and the cost thereof substantially as follows:

1.—Mixing Bowl	$ 445.81
2.—Expander Screens	18.19
3.—Cat Line Roller	79.38
4.—Window Roller	184.97
5.—Experimental Laboratory	525.58
6.—Bakelite	1,334.72
7.—Wiper	.25
	$2,588.90

It was moved by Mr. Elliott, seconded by Mr. Ballagh, that the President's report of experimental work and the cost thereof, be approved. Motion unanimously carried.

Mr. Rennie recommended that a study be made of the sales and financial condition of the company with a view to establishing an appropriation on a

Plaintiff's Exhibit No. 1—(Continued)

flat basis, or percentage basis, for the development of new items and for sales promotion. It was moved by Mr. Ballagh, seconded by Mr. Elliott, that Mr. Rennie's recommendation be accepted. Motion unanimously carried.

Mr. Rennie was requested to make a detailed report after a study of the sales and financial condition of the company had been made.

It was moved by Mr. Elliott, seconded by Ballagh, that the company appropriate any part up to One Hundred Dollars to protect or to progress with the development of the new expander which Mr. Patterson discussed with the Board. Motion unanimously carried.

It was moved by Mr. Rennie, seconded by Mr. Elliott, that Mr. H. C. Armington be reimbursed by the company for his expenses in connection with engineering work in the development of expanding equipment. Motion unanimously carried.

The Board approved the contribution to the National Association of Manufacturers, authorized by J. C. Ballagh. The Board also approved of the reimbursement to J. C. Ballagh for personal contribution made to the State Chamber of Commerce.

There being no further business to come before the meeting, on motion duly made, seconded and carried, the meeting adjourned.

Attest:

(Sgd) J. C. BALLAGH,
Secretary.

(Sgd) C. L. PATTERSON,
President.

Plaintiff's Exhibit No. 1—(Continued)

MINUTES OF MEETING OF BOARD OF DIRECTORS OF PATTERSON-BALLAGH CORPORATION,

A meeting of the Board of Directors of Patterson-Ballagh Corporation was held at the office and principal place of business of the company, 1900 East 65th Street, Los Angeles, California on the 28th day of November, 1938, at the hour of 8:30 o'clock a. m., pursuant to notice issued.

There were present and acting at said meeting

C. L. Patterson
J. C. Ballagh
E. S. Dulin
H. W. Elliott
J. C. Rennie

being all of the Directors of said corporation.

The President declared a quorom present and called the meeting to order.

The first order of business was the reading of the minutes of the preceding meeting of the Board. The minutes were read and it was moved by Mr. Elliott, seconded by Mr. Rennie, that the minutes be approved as read. Motion unanimously carried.

The balance sheet of the corporation for the month ending October 31, 1938, was presented to the Board by Mr. Patterson. On motion of Mr. Elliott, seconded by Mr. Dulin, and unanimously carried, the statement was received in order to file.

The President reported on experimental work and

Plaintiff's Exhibit No. 1—(Continued)

the cost thereof, for the Month of October, substantially as follows:

1.—Mixing Bowl	$26.83
2.—Window Roller	1.79
3.—Split Sleeve	23.05
4.—Expander Stretcher	47.98
	$99.65

It was moved by Mr. Elliott, seconded by Mr. Dulin, that the President's report of experimental work and the cost thereof, be approved. Motion unanimously carried.

On the unfinished business Mr. Patterson presented to the Board the report of Mr. Rennie of the sales and financial condition of the corporation, which he requested Mr. Rennie to read in its entirety. After a brief discussion, and owing to the fact that there was not enough time to pass on the report at this meeting, it was agreed that the report would be discussed at a meeting to be held on Friday, December, 2, 1938, at 8:30 a. m.

The next matter before the Board was the recommendation of Mr. Rennie regarding the change in the fiscal year to end November 30, 1938, instead of December 31st, as heretofore. It was moved by Mr. Ballagh, seconded by Mr. Elliott, and unanimously carried, that this company make formal application to the Department of Internal Revenue, for the change in the Fiscal Year to end November 30th, and that the officers be instructed to take the necessary steps to accomplish this change.

Plaintiff's Exhibit No. 1—(Continued)

The next matter to come up for discussion was the payment of a bonus to employees. After a general discussion, and upon motion duly made and seconded it was unanimously

Resolved, That the officers of Patterson-Ballagh Corporation work out a fair and equitable basis of bonus to all employees, other than executives, and that the method of working out not be set as a precedent for future years;

Resolved Further, that the amount of bonus to be paid shall not exceed $2500.00, for the eleven months ending November 30, 1938, and shall be payable on December 16, 1938.

The next matter to come up for discussion was presented by Mr. Ballagh in the form of two new items which he suggested could be taken over by Patterson-Ballagh Corporation for sale and service on a royalty basis in the Mid-Continent, and also for export.

1.—The McQuiston Grinder.

2.—The Edwards Wire Rope Clamp.

After a general discussion, it was the concensus of opinion of the board that these two items should be investigated very carefully and an analysis made and presented to the Board before any action was taken.

On motion duly made, seconded and carried, the meeting adjourned at 9:40 a. m.

(Sgd) J. C. BALLAGH,
Secretary.

(Sgd) C. L. PATTERSON,
President.

Plaintiff's Exhibit No. 1—(Continued)

MINUTES OF MEETING OF BOARD OF DIRECTORS OF PATTERSON-BALLAGH CORPORATION

A meeting of the Board of Directors of Patterson-Ballagh Corporation was held at the office and principal place of business of the company, 1900 East 65th Street, Los Angeles, California on the 2nd day of December, 1938, at the hour of 8:30 a. m., as agreed at the previous meeting.

There were present and acting at said meeting

C. L. Patterson
J. C. Ballagh
E. S. Dulin
H. W. Elliott
J. C. Rennie

being all of the Directors of said corporation.

The President declared a quorum present and called the meeting to order.

The first order of business was the reading of the minutes of the preceding meeting of the Board. The minutes were read and it was moved by Mr. Elliott, seconded by Mr. Rennie, that the minutes be approved as read. Motion unanimously carried.

The first matter to be discussed was the overtime payment to employees affected by the Fair Labor Standards Act of 1938. It was moved by Mr. Renee, seconded by Mr. Dulin, and unanimously carried, that the following Resolution be adopted to supersede the Resolution adopted at the meeting held September 27, 1938:

Plaintiff's Exhibit No. 1—(Continued)

Resolved, That all office employees of this corporation be employed on the basis of a 40-hour week, with time and one-half for all overtime worked over 44 hours in any one week;

Resolved Further, That the salary of each such employee shall be equal in amount on a 40 hour basis to that paid prior to October 1, 1938, and that any overtime paid for the period October 1st to November 30, 1938, be and it is hereby approved.

A discussion was had relative to a donation to the Community Chest and it was unanimously agreed that a contribution equal to that made last year should be forwarded to the Community Chest.

On the unfinished business the report of Mr. Rennie, of the sales and financial condition of the corporation, was presented for discussion. In order to avoid a prolonged discussion it was agreed to take one item at a time until the entire report was covered.

The first item up for discussion was Gross Profit from Manufacturing and the practicability of running the business strictly on a poundage basis. It was moved by Mr. Dulin, seconded by Mr. Elliott, that the executive officers review the price situation, also review prices for the coming year, and that the comments as set forth by Mr. Rennie in his report be given careful consideration. Motion unanimously carried.

The next item discussed was the Selling Expense. This item was discussed at great length, particular-

Plaintiff's Exhibit No. 1—(Continued)

ly in regard to Mr. J. M. O'Melveny's expenses, and the Cigar Account. It was moved by Mr. Dulin, seconded by Mr. Elliott, that a study of these expenses should be made by the man in charge (J. C. Ballagh) to determine what reductions could be made, and to report the result of his findings at the next meeting.

The Telephone and Telegraph Account, together with the Advertising Account, were next discussed, and it was the concensus of opinion of all the directors that these accounts were high and that every effort should be made to cut them down.

Mr. Rennie left the meeting at this point while the Board discussed the matter of his employment by the company.

After a general discussion regarding Mr. Rennie's employment Mr. Dulin stated that before he, as a director, would be agreeable to making this sort of a deal, he would like to have an opportunity to review the matter in further detail.

On motion duly made, seconded and carried, the meeting adjourned at 9:55 a. m.

(Sgd) J. C. BALLAGH,
Secretary.

(Sgd) C. L. PATTERSON,
President.

Plaintiff's Exhibit No. 1—(Continued)

MINUTES OF MEETING OF BOARD OF DIRECTORS OF PATTERSON-BALLAGH CORPORATION

A meeting of the Board of Directors of Patterson-Ballagh Corporation was held at the office and principal place of business of the company, 1900 East 65th Street, Los Angeles, California, on the 20th day of December, 1938, at the hour of 8:30 o'clock a. m., pursuant to notice issued.

Present: C. L. Patterson
J. C. Ballagh
H. W. Elliott
J. C. Rennie

Absent: E. S. Dulin

The President declared a quorum present and called the meeting to order.

The first order of business was the reading of the minutes of the preceding meeting of the Board. The minutes were read and it was moved by Mr. Elliott, seconded by Mr. Rennie, that the minutes be approved as read. Motion unanimously carried.

The President reported on experimental work and the cost thereof, for the month of November, substantially as follows:

1.—Mixing Bowl	$112.77
2.—Catline Roller	9.62
3.—Expander Stretcher	175.33
Total	$297.72

Plaintiff's Exhibit No. 1—(Continued)

It was moved by Mr. Elliott, seconded by Mr. Rennie, that the President's report of experimental work and the cost thereof, be approved. Motion unanimously carried.

On the unfinished business, Mr. Ballagh reported that while in Houston he had apprised Mr. O'Melveny of the fact that the Board considered his expenses to be exorbitant and that every effort should be made to reduce this item. Mr. Ballagh stated that what he had in mind was a budget plan which would be gone over by Mr. Rennie with Mr. O'Melveny when he came to California after the first of the year. The subject was discussed at length and it was unanimously agreed to carry the matter over as unfinished business.

The next item was the McQuiston Grinder. Mr. Ballagh reported that he had investigated the possibilities of this item in the Mid-Continent and felt sure that there was some money to be made on the item but was not yet fully satisfied that we were going into it on the right basis. After a general discussion it was unanimously agreed to carry the matter over as unfinished business.

The Edwards Dead Line Rope Clamp and Storage Reel was discussed next. Mr. Ballagh reported that he had investigated the possibilities of this item in the Mid-Continent and recommended that Patterson-Ballagh Corporation enter into negotiations with E. H. Edwards Company for the handling of this item. It was moved by Mr. Ballagh, seconded by Mr. Elliott, and unanimously car-

Plaintiff's Exhibit No. 1—(Continued)

ried, that Patterson-Ballagh Corporation acquire the exclusive manufacturing and sales rights, including export, for the Edwards Dead Line Rope Clamp and Storage Reel on a royalty of five (5) per cent of cash receipts from sales, without any minimum sales requirement or guarantee.

Mr. Patterson stated it had been suggested by Mr. Rennie that he would prefer to have Miss Nolan excused from the meeting at this point.

Mr. Patterson then made a motion that Mr. Rennie be appointed Office Manager in charge of all office work, all office employees, all records of the corporation, with power to hire and fire employees, at a salary of $400.00 per month, effective December 1, 1938.

After a discussion as to the extent of this authority, Mr. Elliott remarked that this was more authority than had been given anyone else in the organization, and he inquired whether this authority was to extend to the office in Houston, which Mr. Patterson said was the intention.

Mr. Ballagh then stated that when this matter was discussed at a previous meeting, Mr. Dulin had expressed the wish to have the matter of Mr. Rennie's employment held over until a later meeting to allow him time to study it over. Mr. Ballagh further stated that, inasmuch as Mr. Dulin was not present to vote, he preferred to not vote on the question.

Mr. Elliott stated that, inasmuch as the matter concerned Mr. Rennie, he (Mr. Rennie) could not

Plaintiff's Exhibit No. 1—(Continued)

vote on the matter, and he, Mr. Elliott, and Mr. Patterson together did not constitute a quorum, and, therefore, the matter could not be voted upon. The matter was then tabled, to be brought up at the next meeting.

On motion duly made, seconded and carried, the meeting adjourned at 10:30 a. m.

(Sgd) J. C. BALLAGH,
Secretary.

(Sgd) C. L. PATTERSON,
President

MINUTES OF ANNUAL MEETING OF STOCKHOLDERS OF PATTERSON-BALLAGH CORPORATION

The annual meeting of the stockholders of Patterson-Ballagh Corporation was held at the office and principal place of business of the company, 1900 East 65th Street, Los Angeles, California, on the 27th day of January, 1939, at the hour of 8:30 o'clock a. m., pursuant to notice issued.

The meeting was called to order by Mr. E. S. Dulin, who acted as Chairman of the meeting, and Mr. J. C. Ballagh acted as Secretary.

The Secretary thereupon called the roll of stockholders and the following report was made of stockholders and stock representatives at the meeting:

Plaintiff's Exhibit No. 1—(Continued)

Name	No. of Shares
Ballagh, J. C.	125
Byron Jackson Co., (a corporation) by E. S. Dulin, Pres.	249
Dulin, E. S.	1
Highland Investment Corp., Ltd. by J. C. Ballagh, Pres.	250
Patterson, C. L.	375
Total Capital Stock	1,000

The Secretary reported that the above number of shares represented all of the issued and outstanding stock as of said date.

The Chairman announced that the next business before the meeting was the election of a Board of Directors for the ensuing year.

Upon motion duly made and seconded it was unanimously

> Resolved, That the incumbent Directors be re-elected for the ensuing year, or until their successors are chosen and elected, which act can only be accomplished by the majority approval of the Stockholders.

The financial report of the corporation for the period ending November 30, 1938, as prepared under the direction of the Secretary-Treasurer, was presented and unanimously approved, and a summary of same was ordered attached hereto and made a part of the minutes of this meeting.

There being no further business to come before

Plaintiff's Exhibit No. 1—(Continued)

the meeting, on motion duly made, seconded and carried, it was thereupon adjourned.

.....

Chairman.

(Sgd) J. C. BALLAGH,

Secretary.

PATTERSON-BALLAGH CORPORATION

Secretary's Report of 1938 Operations to November 30, 1938

INCOME and PROFIT and LOSS

Gross Sales		$271,910.78
Cost of Goods Sold	$68,382.43	
Royalties	12,813.13	81,195.56
Gross Profit from Manufacturing		190,715.22
Operating Expenses		150,891.81
Net Income from Operations		39,823.41
Other Expenses—Less Other Income		7,439.07
Net Gain for period, before Income Tax Deduction		32,384.34
Less Estimated Federal & State Taxes		7,087.99
		25,296.35

Summary of Surplus

Balance as per Ledger November 30, 1938		$105,590.46
1938 Credits:		
Net Profit from Operations (before Federal & State Tax)		32,384.34
		137,974.80
1938 Charges:		
Federal Income Tax 1937	4,956.50	
Dividends Paid July 7, 1938	6,000.00	
Accrued Capital Stock Tax	71.00	11,027.50
Total Earned Surplus at 11/30/38		126,947.30

Plaintiff's Exhibit No. 1—(Continued)

Appreciated Surplus		1,611.86
Balance, Surplus as per Ledger 11/30/38		128,559.16
Less Estimated Taxes for 1938:		
Est. Federal Income Tax 1938	5,887.99	
Est. State Franchise Tax 1938	1,200.00	7,087.99
Surplus Balance after Estimated Taxes		$121,471.17

Note: Estimated Federal Income Tax..... 5,887.99
do State Franchise Tax 1,200.00

Total..... 7,087.99 for 1938 operations, payable during 1939. 1938 tax of $4,956.50 has been deducted to show surplus of $128,559.16, as shown on our books. Item of $5,887.99 is chargeable against surplus in 1939, while item of $1,200.00 is chargeable against 1939 Profit and Loss. For this reason net profit from operations is shown before tax.

I, J. C. Ballagh, as Secretary-Treasurer of Patterson-Ballagh Corporation, hereby certify that the foregoing report is true, to the best of my knowledge and belief.

(Sgd) J. C. BALLAGH

MINUTES OF ANNUAL MEETING OF DIRECTORS OF PATTERSON-BALLAGH CORPORATION

The annual meeting of the directors of Patterson-Ballagh Corporation was held at the office and principal place of business of the company, 1900 East 65th Street, Los Angeles, California, on the 27th day of January, 1939, immediately following the annual meeting of the stockholders.

Plaintiff's Exhibit No. 1—(Continued)

Present:

C. L. Patterson
J. C. Ballagh
E. S. Dulin
J. C. Rennie

Absent:

H. W. Elliott

The meeting was called to order *Mr.* Mr. E. S. Dulin, who acted as Temporary Chairman of the meeting, and Mr. J. C. Ballagh acted as Secretary.

The Chairman stated that the first business to come before the meeting was the election of officers for the ensuing year, or until their successors are chosen, appointed and elected by the Board. On motion made and seconded the following officers were nominated for re-election:

C. L. Patterson, President
J. C. Ballagh, Secretary-Treasurer
M. G. Nolan, Asst. do

A vote was had on the nominations of the above named persons, and the results were as follows:

E. S. Dulin .....Yes
C. L. Patterson .....Yes
J. C. Rennie .....Yes
J. C. Ballagh ..... No

The Chairman thereupon passed the meeting over to Mr. Patterson, with the proviso that the records show Mr. Ballagh's reason for voting 'no'.

MR. Ballagh: "I am voting 'no' pending an agreement with Mr. Patterson as to the dele-

Plaintiff's Exhibit No. 1—(Continued)

gation of authority between us. I am asking that this matter be again brought up at the next directors' meeting, at which Mr. Elliott is present. For ten years the corporation has operated with an equal flow of authority as between Petterson and myself. Mr. Patterson refuses at this time to agree to the fact that the President and Secretary of Patterson-Ballagh Corporation have equal authority in the operation of the corporation."

The Directors were asked if they wished to change their vote after having heard Mr. Ballagh's statement. Mr. Dulin, Mr. Patterson and Mr. Rennie voted the same. Mr. Rennie further stated that until other facts were known, or until he had reason to change his opinion one way or the other, he would vote as he had voted

The next matter of business was the discussion of Mr. Rennie's employment with the company.

Upon motion duly made and seconded, the following Resolutions were unanimously adopted:

Resolved, That Mr. Rennie be instructed by the Board to render a report to the individual members of the Board by February 8th, and that such report shall be the basis of full discussion and disposition by the Board at a meeting on February 10th, and that this report shall contain among other things, the following:

(1) A proposed budget for the year 1939, both income and expenditures.

(2) An analysis of the efficiency of the

Plaintiff's Exhibit No. 1—(Continued)

operations of the office, together with any suggestions for change in personnel of the office force, or changes in compensation, and that such information or suggestions be obtained from any officer or department head, and that any one, either officer or employee, who does not cooperate fully upon same, that particular party shall be reported to the Board.

Resolved Further, That the arrangement with Mr. Rennie be continued on a temporary basis until the above mentioned report is rendered and the Board takes action on it, at which time the Board is to determine definitely Mr. Rennie's status and set his compensation.

On motion of Mr. Dulin, seconded by Mr. Ballagh, and unanimously passed, the following resolutions were adopted:

Resolved, that the officers' salaries, viz: Mr. Patterson and Mr. Ballagh, be each One Thousand ($1,000.00) Dollars per month, effective January 1, 1939.

Resolved, That all company correspondence shall be placed in the company files. Correspondence from officers shall be placed in separate files, available to officers and directors.

The next matter to be discussed was the sale of Patterson-Ballagh Wire Line Guides to Medearis Oilwell Supply Company. It was unanimously agreed that they be allowed to buy on the basis of a regular supply store.

Plaintiff's Exhibit No. 1—(Continued)

The proposed resolution regarding the Experimental Department, as offered by Mr. Ballagh, was tabled until the report to be presented by Mr. Rennie was received.

The matter of the McQuiston Grinder and the deal with the Oil Well Supply Company on the Swivel Bumper were tabled until the next meeting.

On motion duly made, seconded and carried, the meeting adjourned at 11:30 a. m.

(Sgd) J. C. BALLAGH
Secretary

(Sgd) C. L. PATTERSON
Chairman

MINUTES OF MEETING OF BOARD OF DIRECTORS OF PATTERSON-BALLAGH CORPORATION

A meeting of the Board of Directors of Patterson-Ballagh Corporation was held at the office and principal place of business of the company, 1900 East 65th Street, Los Angeles, California, on the 10th day of February, 1939, at the hour of 8:30 o'clock a. m., as agreed at the previous meeting.

There were present and acting at said meeting

C. L. Patterson
J. C. Ballagh
E. S. Dulin
H. W. Elliott
J. C. Rennie

being all of the Directors of said corporation.

Plaintiff's Exhibit No. 1—(Continued)

The President declared a quorum present and called the meeting to order.

The first order of business was the reading of the minutes of the preceding meeting of the Board. The minutes were read and it was moved by Mr. Dulin, seconded by Mr. Elliott, that the minutes be approved as corrected. Motion unanimously carried.

The matter of the re-election of officers for the ensuing year was reviewed, and Mr. Ballagh withdrew his objections as expressed at the previous meeting.

The budget of income and expenditures for the year 1939, as prepared by Mr. Rennie, was received and presented for discussion. It was the concensus of opinion that certain items,—viz: advertising, selling expense, donations, subscriptions to various publications, et cetera, were too high.

It was moved by Mr. Dulin, seconded by Mr. Ballagh, that the officers of the corporation, assuming their projected sales to be as set forth in the report, handle their expenses and revise the budget to show a gross profit of $50,000.00. Motion unanimously carried.

It was suggested by Mr. Dulin that immediate steps be taken to effect this change.

The next matter to be discussed was the report of Mr. Rennie on the efficiency of the operations of the office, as requested at the previous meeting.

At this point Mr. Ballagh announced that he and Mr. Patterson were working on a plan which they

Plaintiff's Exhibit No. 1—(Continued)

hoped would be of benefit to the company, and that they would probably be ready to present this plan to the Board within a few days. It was unanimously agreed to have a meeting of the Board of Directors not later than February 17th.

The proposed deal with the Oil Well Supply Company, regarding Swivel Bumpers, was discussed. It was moved by Mr. Dulin, seconded by Mr. Ballagh, that a deal be worked out with the Oil Well Supply Company on a unit royalty basis, instead of granting a paid up license. Motion unanimously carried.

On motion duly made, seconded and carried, the meeting adjourned at 10:45 a. m.

(Sgd) J. C. BALLAGH
Secretary

(Sgd) C. L. PATTERSON
President

MINUTES OF SPECIAL MEETING OF BOARD OF DIRECTORS OF PATTERSON-BALLAGH CORPORATION

A special meeting of the Board of Directors of Patterson-Ballagh Corporation was held on the 15th day of February, 1939, at 1900 East 65th Street, Los Angeles, California, at the hour of 4:00 o'clock P. M. of said day, pursuant to the Consent to Hold and Waiver of Notice signed by all of the Direc-

Plaintiff's Exhibit No. 1—(Continued)

tors and hereinafter in the minutes of the meeting contained.

Directors Present:

J. C. Ballagh
E. S. Dulin
C. L. Patterson
J. C. Rennie

Directors Absent:

H. W. Elliott

Also present:

Howard Burrell
D. G. Miller

The Consent to Hold and Waiver of Notice, which was signed by each and every Director of the corporation is as follows:

CONSENT TO HOLD AND WAIVER OF NOTICE OF SPECIAL MEETING OF BOARD OF DIRECTORS OF PATTERSON-BALLAGH CORPORATION

Know All Men by These Presents:

That we, the undersigned, being all of the Directors of Patterson-Ballagh Corporation, by mutual consent and understanding beforehand, hereby consent to hold a special meeting of the Board of Directors of said corporation at 1900 East 65th Street, Los Angeles, California, on the 15th day of February, 1939, at the hour of 4:00 o'clock P. M. of said

Plaintiff's Exhibit No. 1—(Continued)

day, and we agree that all the acts and proceedings of said meeting shall be as valid as if had or taken at a meeting duly and regularly called and noticed.

We further waive all notice of the time, place and purpose of said meeting, whether required by the By-Laws of this corporation, or otherwise.

In Witness Whereof, we have hereunto subscribed our signatures this 15th day of February, 1939.

(Sgd) C. L. PATTERSON
(Sgd) H. W. ELLIOTT
(Sgd) J. C. BALLAGH
(Sgd) E. S. DULIN
(Sgd) J. C. RENNIE

Reading of Minutes

The President called the meeting to order and presided thereover until his retirement therefrom. He announced that the first business before the same was a consideration of the minutes of the meeting of the Board of Directors held on the 10th day of February, 1939, and, thereupon, on motion of Director Dulin, seconded by Director Ballagh and unanimously carried, the matter of the consideration of said minutes was postponed until the next meeting of the Board of Directors for the purpose of conserving time.

Resignation of J. C. Rennie

There was then presented to the meeting the resig-

Plaintiff's Exhibit No. 1—(Continued)

nation of J. C. Rennie as a Director of the corporation, which read as follows:

"Los Angeles, California
January 27, 1939

To the Board of Directors
Patterson-Ballagh Corporation
Los Angeles, California

Gentlemen:

I herewith tender my resignation as a Director of Patterson-Ballagh Corporation, to take effect at the pleasure of the Board of Directors and majority approval of the Stockholders of the Corporation.

Very truly Yours
J. C. RENNIE"

Approved 2/15/39
C. L. PATTERSON
By DE MONT G. MILLER proxy
J. C. BALLAGH

HIGHLAND INVESTMENT CO. LTD.
J. C. BALLAGH,
Pres.

It was pointed out that a majority of the shareholders had approved the resignation and, thereupon, on motion of Director Ballagh, second by Director Patterson and carried, Director Dulin voting in the negative, it was

Resolved, that the resignation of J. C. Rennie as a Director of this corporation presented at

Plaintiff's Exhibit No. 1—(Continued)

this meeting shall be and the same is hereby accepted.

Compensation of J. C. Rennie

Director Ballagh discussed the matter of terminating the services of J. C. Rennie with the corporation and presented a check covering the same to the date of the meeting. A discussion followed as to the terms of hiring under which he had been employed and it was the concensus of opinion that the employment should be terminated as at the close of business on February 28, 1939, and that J. C. Rennie be given immediate notice thereof.

Thereupon, on motion of Director Ballagh, seconded by Director Patterson and carried, Director Dulin voting in the negative, it was

Resolved, that this corporation terminate the employment of J. C. Rennie as at the close of business on February 28, 1939, and that he be given immediate notice of such action and be paid his regular compensation for the month of February, as in the past, upon his rendition of the services contemplated in his employment.

Thereupon, J. C. Rennie was advised of the action of the Board in respect to his resignation and the termination of his employment and retired from the meeting.

Election of De Mont G. Miller

The meeting then considered the matter of the election of a Director to fill the vacancy created by

Plaintiff's Exhibit No. 1—(Continued)

the resignation of J. C. Rennie, and Director Ballagh nominated De Mont G. Miller as a Director to fill such vacancy.

Thereupon, on motion of Director Ballagh, seconded by Director Dulin and unanimously carried, it was

Resolved, that the nominations be closed and that De Mont G. Miller shall be and he is hereby elected and appointed as a Director of this corporation to fill the vacancy created by the resignation of J. C. Rennie, to be effective immediately.

Resignation of C. L. Patterson

There was then presented to the meeting the resignation of C. L. Patterson as the President and a Director of the corporation, which read as follows:

"Los Angeles, California
Feb 15 - 1939.

Patterson-Ballagh Corporation
Los Angeles, California

Gentlemen:

The undesigned hereby tenders his resignation as the President and a Director of Patterson-Ballagh Corporation, the same to take effect immediately upon delivery hereof to you.

Very truly yours,
C. L. PATTERSON"

Thereupon, on motion of Director Ballagh, sec-

Plaintiff's Exhibit No. 1—(Continued)

onded by Director Dulin and unanimously carried, it was

> Resolved, that the resignation of C. L. Patterson as the President and a Director of this corporation, presented at this meeting, shall be and the same is hereby accepted.

Thereupon, C. L. Patterson retired from the Chair and the meeting and Director Ballagh took the Chair and presided over the meeting until the election of a President to fill the vacancy created by the resignation of C. L. Patterson.

Communication from C. L. Patterson

C. L. Patterson then delivered to and left with the Directors a communication addressed to the corporation, advising of his execution of an option and agreement with DeMont G. Miller covering the sale and purchase of the shares of the capital stock of the corporation held by him and calling attention to an agreement between him and DeMont G. Miller in respect to the application of dividends declared on the shares covered by the option agreement during the existence thereof.

Election of President

The meeting then proceeded with the matter of electing a President of the corporation to fill the vacancy existing in said office, and Director Ballagh placed the name of Director Miller in nomination.

There being no further nominations, on motion of Director Ballagh, seconded by Director Dulin and unanimously carried, it was

> Resolved, that the nominations be closed and

Plaintiff's Exhibit No. 1—(Continued)

that De Mont G. Miller shall be and ie hs hereby elected and appointed as the President of this corporation to fill the vacancy caused by the resignation of C. L. Patterson, to be effective immediately.

Thereupon, Director Ballagh retired from the Chair and Director Miller, as the President of the corporation, took the same and presided over the meeting during the balance thereof.

Election of H. C. Armington

The meeting then proceeded with the matter of electing a Director to fill the vacancy created by the resignation of C. L. Patterson as such, and Director Ballagh placed the name of H. C. Armington in nomination.

There being no further nominations, on motion of Director Ballagh, seconded by Director Dulin and unanimously carried, it was

Resolved, that H. C. Armington shall be and he is hereby elected and appointed as a Director of this corporation to fill the vacancy created by the resignation of C. L. Patterson as such, to be effective immediately.

Compensation of President

The meeting then proceeded with the matter of considering the compensation to be paid to the President for his services and the advisability of designating him as General Manager of the business and affairs of the corporation. The suggestion was made that such compensation be fixed in the same

Plaintiff's Exhibit No. 1—(Continued)

amount as had been paid the former President since the first of the current year.

Thereupon, on motion of Director Ballagh, seconded by Director Dulin and unanimously carried, it was

> Resolved, that the President of this corporation shall be the General Manager of its business and affairs and that he shall receive as compensation for his services commencing as of February 15, 1939, the sum of $1,000.00 a month, payable in the same manner and on the same dates as other executive salaries.

Checks and Drafts

It was called to the attention of the meeting that the authority of C. L. Patterson to sign checks and drafts on the bank account of the corporation should be revoked by reason of his retirement therefrom and that the President and General Manager should be given the same authority in this respect as had formerly been vested in C. L. Patterson.

Thereupon, on motion of Director Ballagh, seconded by Director Dulin and unanimously carried, it was

> Resolved, that the authority heretofore given to C. L. Patterson to sign checks and drafts for and on behalf of this corporation shall be and the same is hereby terminated and rescinded immediately and that all depositaries of the funds of this corporation shall be advised at once of the termination and rescission of said authority.

Plaintiff's Exhibit No. 1—(Continued)

Further Resolved, that De Mont G. Miller shall be authorized to sign checks and drafts on the funds of this corporation in the same manner and to the same extent as C. L. Patterson has been authorized so to do and that the depositaries of the funds of this corporation shall be advised of the authority herein placed in De Mont G. Miller.

Adjournment

There being no further business, on motion, duly seconded and unanimously carried, the meeting was adjourned.

(Sgd) J. C. BALLAGH
Secretary

Los Angeles, California
February 15, 1939.

Patterson-Ballagh Corporation,
1900 East 65th Street
Los Angeles, California

Gentlemen:

The undersigned wishes to advise that he has made and executed with De Mont G. Miller an option and agreement covering the sale and purchase of the shares of the capital stock of Patterson-Ballagh Corporation held by him, and there is being forwarded to you herewith a copy of his said agreement for your files.

Mr. De Mont G. Miller has paid to the undersigned or for his account the sum of $2,500.00 mentioned in paragraph First of the agreement and

Plaintiff's Exhibit No. 1—(Continued)

the sum of $7,500.00 mentioned in paragraph Fourth thereof, and has executed and delivered the promissory note in said latter paragraph contemplated. You are also advised that the stock certificates mentioned in the agreement have been delivered by Security-First National Bank of Los Angeles to De Mont G. Miller and he has deposited them with said bank as collateral security for the performance of his obligations provided in his promissory note.

You are therefore advised and instructed to pay to De Mont G. Miller all dividends up to and including the amount of $6.00 per share declared in any calendar year on the shares evidenced by the certificates mentioned in said agreement and not transferred on your books and records to him unless you shall be hereafter advised and instructed to the contrary. You will of course pay all dividends in excess of $6.00 per share declared in any calendar year on said shares to Security-First National Bank of Los Angeles, Seventh and Spring Streets office, for the account of the undersigned to be credited on the obligations of De Mont G. Miller as in said agreement provided.

Very truly yours,

(Sgd) C. L. PATTERSON

Plaintiff's Exhibit No. 1—(Continued)

Los Angeles, California
Feb 15 - 1939.

Patterson-Ballagh Corporation,
Los Angeles, California

Gentlemen:

The undersigned hereby tenders his resignation as the President and a Director of Patterson-Ballagh Corporation, the same to take effect immediately upon delivery hereof to you.

Very truly yours,
(Sgd) C. L. PATTERSON

Los Angeles, California,
January 27, 1939.

To the Board of Directors
Patterson-Ballagh Corporation
Los Angeles, California

Gentlemen:

I herewith tender my resignation as a Director of Patterson-Ballagh Corporation, to take effect at the pleasure of the Board of Directors and majority approval of the Stockholders of the Corporation.

Very truly yours,
(Sgd) J. C. RENNIE,
Approved 2/15/39
C. L. PATTERSON,
(Sgd) By DeMONT G. MILLER,
Proxy,
(Sgd) J. C. BALLAGH,
Highland Investment Co., Ltd.
(Sgd) J. C. BALLAGH,
President.

Plaintiff's Exhibit No. 1—(Continued)

Los Angeles, California
February 14, 1939.

To the Board of Directors of
Patterson-Ballagh Corporation

I, H. W. Elliott, do hereby tender my resignation as a director of Patterson-Ballagh Corporation to take effect immediately.

(Sgd) H. W. ELLIOTT.

MINUTES OF SPECIAL MEETING OF BOARD OF DIRECTORS OF PATTERSON-BALLAGH CORPORATION

A special meeting of the Board of Directors of Patterson-Ballagh Corporation was held on the 27th day of June, 1939, at 1900 East 65th Street, Los Angeles, California, at the hour of 2:00 o'clock P. M. of said day, pursuant to notice duly and regularly given to each of the Directors in accordance with the By-Laws of the corporation.

Directors Present:

H. C. Armington
J. C. Ballagh
E. S. Dulin
D. G. Miller

Directors Absent:

H. W. Elliott

Also Present:

Howard Burrell

Plaintiff's Exhibit No. 1—(Continued)

Certificate of Notice

The President called the meeting to order and presided thereover. The Secretary presented his certificate to the effect that due and regular notice of the meeting had been given to each of the Directors, in accordance with the By-Laws of the corporation, and it was ordered that the same be placed in the minute book immediately following the minutes of this meeting.

Reading of Minutes

The next order of business was the consideration of the minutes of the special meeting of the Board of Directors held on the 15th day of February, 1939. The Secretary presented said minutes and Director Dulin stated that the same should be changed to indicate that the communication dated February 15, 1939, from C. L. Patterson to the corporation was delivered to and left with the Directors, instead of being presented and read.

Thereupon, on motion of Director Dulin, seconded by Director Ballagh and unanimously carried, it was

> Resolved, that the minutes of the special meeting of the Board of Directors of this corporation held on the 15th day of February, 1939, shall be and the same are hereby approved as as modified by the changing thereof to indicate that C. L. Patterson delivered to and left with the Directors his communication to the corporation of said date.

Plaintiff's Exhibit No. 1—(Continued)

Communication from C. L. Patterson

The communication dated February 15, 1939, from C. L. Patterson to the corporation in respect to the option agreement executed between him and De Mont G. Miller, covering the sale and purchase of the shares of capital stock held by C. L. Patterson was then read to the meeting and it was ordered that the same be placed in the minute book of the corporation immediately following the minutes of this meeting.

Resignation of H. W. Elliott

There was then presented to the meeting the resignation of H. W. Elliott as a Director of the corporation, which was dated February 14, 1939, and by its terms was to take effect immediately. The resignation was as follows:

"Los Angeles, California
February 14, 1939

To the Board of Directors of
Patterson-Ballagh Corporation

I, H. W. Elliott, do hereby tender my resignation as a director of Patterson-Ballagh Corporation to take effect immediately.

H. W. ELLIOTT"

Thereupon, on motion of Director Ballagh, seconded by Director Armington and unanimously carried, it was

Resolved, that the resignation of H. W. Elliott as a Director of this corporation, presented at this meeting, shall be and the same is hereby accepted with regret.

Plaintiff's Exhibit No. 1—(Continued)

Election of Howard Burrell

The meeting then proceeded with the matter of electing a Director to fill the vacancy created by the resignation of H. W. Elliott as such, and Director Ballagh placed the name of Howard Burrell in nomination.

There being no further nominations, on motion of Director Ballagh, seconded by Director Dulin and unanimously carried, it was

> Resolved, that Howard Burrell shall be and he is hereby elected and appointed as a Director of this corporation to fill the vacancy created by the resignation of H. W. Elliott as such, to be effective immediately.

Communication from President

The President then read to the meeting a letter covering the situation in respect to the alleged obligation of the company to pay royalties to Byron Jackson Co. on protectors manufactured and sold by it. At the conclusion of the presentation of said letter he read to the meeting a letter from Musick and Burrell dated June 23, 1939, containing an opinion to the effect that from the data submitted to said firm it was of the opinion that the company could legally renounce and terminate the agreement dated September 20, 1928, executed with Byron Jackson Pump Company, on the grounds of the invalidity of the Bettis and Hopkins patents mentioned therein. A discussion of the problem followed and it was ordered that the communication from the President to the Board of Directors and

Plaintiff's Exhibit No. 1—(Continued)

the letter to the company from Musick and Burrell be placed in the minute book immediately following the minutes of this meeting.

At the conclusion of said discussion, on motion of Director Burrell, seconded by Director Armington and carried, Director Dulin voting in the negative, the following resolution was adopted:

> Resolved, that the President of this corporation shall be and he is hereby authorized at such time as he may deem advisable to renounce and terminate the agreement dated September 20, 1928, executed by and between Byron Jackson Pump Co., a corporation, as Licensor, and this company, as Licensee, and such other agreements as may be supplemental thereto or connected therewith, and in connection with said renunciation and termination to do and perform such things and take such action as he may consider necessary or proper and to the best interests of this corporation;
>
> Further Resolved, that the President of this corporation shall be and he is hereby instructed to report to this Board such action as he has taken from time to time pursuant to the authority given in the foregoing resolution.

General Problems

The meeting then proceeded with a discussion of the general business problems of the company and its financial statement showing its condition as at May 31, 1939, and the result of its operations during the first six months of the current fiscal year. A dis-

Plaintiff's Exhibit No. 1—(Continued)

cussion also was had on the subject of the amount of business done by the company with other items than protectors and the statement was made that approximately 20% of the gross volume of the business was derived from the handling of such other items.

Adjournment

There being no further business, on motion, duly seconded and unanimously carried, the meeting was adjourned.

(Sgd) J. C. BALLAGH,
Secretary.

Approved:

(Sgd) D. G. MILLER,
President.

Los Angeles, California.
June 27, 1939.

Board of Directors
Patterson-Ballagh Corporation
Los Angeles, California

Gentlemen:

Since assuming office as President of Patterson-Ballagh Corporation I have taken upon myself the duty of studying the various costs in connection with the conduct of this business. I find that for the first six months of 1939 the corporation will show a loss of some $2,000.00. In this study of the various costs I noted the fact that the payment to Byron Jackson Company of royalties under the license agreement was a very substantial sum, and much more than

Plaintiff's Exhibit No. 1—(Continued)

made up the difference between profit and loss to the corporation.

A study of the situation shows that the Bettis patent has been invalidated, and we are no longer operating thereunder. We have, however, been paying royalties to Byron Jackson Company on the protectors, although we have not had any protection or benefit which would flow from a patent. Substantially all of our competitors on the other hand are not under the burden of paying royalties. The payment of these royalties on an unpatented product has been an important factor in the sale of protectors, particularly in the export trade. As stated, these royalty payments mean the difference between operating at a profit or a loss, and it may ultimately drive us out of the export trade.

The facts show that our sales of Patterson-Ballagh protectors to be used in connection with the so-called Hopkins cushion joint have been so small as not to warrant the time and expense involved, and because it has been assumed that the payment of royalties on the unpatented protectors is tied into the license agreement, the result has been a continuous loss.

Because of all this, I asked the firm of Musick and Burrell to make a study of the situation to see if there was not some means by which payment under this agreement could be eliminated. They made an analysis of the situation and prepared a memorandum which is being presented at this meeting. As a result of this analysis and this memorandum, I

Plaintiff's Exhibit No. 1—(Continued)

asked the Secretary to send out notice calling a meeting of the Board of Directors in order to consider this matter at greater length.

Very truly yours,

(Sgd) D. G. MILLER.

(On letterhead of:)

Law Offices
MUSICK AND BURRELL

(Received Stamp:) Jun. 26, 1939 Received

1175 Subway Terminal Building,
Los Angeles, California.

June 23, 1939.

Patterson-Ballagh Corporation
1900 East 65th Street
Los Angeles, California

Attention: Mr. D. G. Miller

Dear Sirs:

At your request we have examined and considered the several agreements between your corporation and Byron Jackson Pump Company, and its successor Byron Jackson Company. We find it necessary to mention only the following agreements:

1. Agreement dated September 20, 1928, whereby Byron Jackson Pump Company purports to grant to your corporation the exclusive right to manufacture and sell the cushion joint claimed to be covered by Hopkins patent No. 1,619,728 upon payment of the royalties as therein provided.

2. Agreement dated September 20, 1928, where-

Plaintiff's Exhibit No. 1—(Continued)

by your corporation purports to grant to Byron Jackson Pump Company an exclusive paid-up license to make and sell and to grant licenses to others to make and sell the parts of the Hopkins device made of steel or other metals.

3. The form of licenses to others signed by Patterson-Ballagh Corporation and Byron Jackson Company, therein "styled the Licensors," and in each instance the named licensee. This agreement among other things provides that Patterson-Ballagh Corporation agrees to sell to the licensee and the licensee agrees to buy from your corporation only the rubbers therein called "Patterson-Ballagh Protectors."

This agreement is
also a license by Byron Jackson Company granting to the licensee the non-exclusive right to make and sell cushion joints for rotary drill pipes described and claimed in said Hopkins patent, subject to the agreement that the rubbers used therein must be bought from Patterson-Ballagh Corporation. No part of the royalty therein reserved is payable to your corporation. No special mention need be made of the other provisions of this agreement.

From our examination of the agreements specified above, as well as the other agreements called to our attention, it is our opinion that your corporation has the right to renounce and terminate, and should give notice to Byron Jackson Company of renunciation and termination of, the agreement of September 20, 1928, first above mentioned and all rights thereunder.

Plaintiff's Exhibit No. 1—(Continued)

You will also by notice release Byron Jackson Company from all obligation to purchase rubbers and cushions described in and as provided by the second agreement mentioned above. The notice must similarly refer to the Letter Agreement of December 22, 1931, signed by Byron Jackson Company and approved December 29, 1931, by Patterson-Ballagh Corporation, J. C. Ballagh and C. L. Patterson. Any licensee under the third agreement mentioned above should be noteified by you of the fact of said renunciation, and should be further notified that he is released from all obligation to purchase the rubber rings exclusively from you. After notice of renunciation your corporation should make no further payment of the royalties specified in the agreement first above mentioned. You should pay or tender to pay all royalties accrued to the date of service of notice of renunciation. It is our opinion that after notice of said renunciation, your corporation may freely manufacture and sell the Bettis protector, or any other protector, without payment of royalty, and that this is true also of the rubber rings used as a part of the Hopkins device, although as to the latter you will be called upon in any litigation to establish the invalidity of the Hopkins patent. We will be pleased to furnish you the form of the notices required to be served.

Very truly yours,

MUSICK AND BURRELL,

(Sgd) By HOWARD BURRELL.

Plaintiff's Exhibit No. 1—(Continued)

MINUTES OF SPECIAL MEETING OF BOARD OF DIRECTORS OF PATTERSON-BALLAGH CORPORATION

A special meeting of the Board of Directors of Patterson-Ballagh Corporation was held on the 22nd day of August, 1939, at 1900 East 65th Street, Los Angeles, California, at the hour of 11:00 o'clock A. M. of said day, pursuant to notice duly and regularly given to each of the Directors in accordance with the By-Laws of the corporation.

Directors Present:

H. C. Armington
J. C. Ballagh
D. G. Miller

Directors Absent:

Howard Burrell
E. S. Dulin

Affidavit of Notice

The President called the meeting to order and presided thereover. The Secretary presented his affidavit to the effect that due and regular notice of the meeting had been given to each of the Directors in accordance with the By-Laws of the corporation, and it was ordered that the same be placed in the minute book immediately following the minutes of this meeting.

Approval of Minutes

The next order of business was a consideration

Plaintiff's Exhibit No. 1—(Continued)

of the minutes of the special meeting of the Board of Directors held on the 27th day of June, 1939. The Secretary presented said minutes and there being no errors or omissions noted therein the same were approved as read.

Report of President

The President reported that immediately following the special meeting of the Board of Directors held on the 27th day of June, 1939, he had caused notices to be sent to Byron Jackson Co., J. C. Ballagh and C. L. Patterson advising of the renunciation and termination by the company of the agreement dated September 20, 1928, executed between Byron Jackson Pump Co., as licensor, and this company, as licensee. It was also reported that the company was in receipt of a communication from Byron Jackson Co., advising that said corporation did not acquiesce in and refused to accept the renunciation and termination of said agreement. It was the consensus of the opinion of the Directors present that the action of the President taken pursuant to the resolutions of the Board of Directors in respect to the renunciation and termination of the Byron Jackson Co. license agreement was proper and satisfactory.

Compensation of Secretary and Treasurer

The meeting then proceeded with a discussion of the amount of compensation being paid by the company to J. C. Ballagh as its Secretary and Treasurer, and the recommendation was made that

Plaintiff's Exhibit No. 1—(Continued)

his salary as such officer be increased to the extent of $4,000.00 per year as of March 1, 1939, on a basis whereby said increase would be paid in four equal quarterly installments commencing on June 1, 1939, and continuing until further order of the Board.

Thereupon, on motion of Director Armington, seconded by Director Miller and carried, Director Ballagh not voting thereon, it was

> Resolved, that commencing as of March 1, 1939, the compensation being paid by this corporation to J. C. Ballagh as its Secretary and Treasurer shall be and the same is hereby increased to the extent of $4,000.00 per year on a basis whereby such increase shall be paid in equal quarterly installments of $1,000.00 each, commencing on June 1, 1939, and continuing until further action of this Board.

Adjournment

There being no further business to come before the meeting, on motion, duly seconded and unanimously carried, the same was adjourned.

(Sgd) J. C. BALLAGH
Secretary

Approved:

(Sgd) D. G. MILLER
President

Plaintiff's Exhibit No. 1—(Continued)

AFFIDAVIT OF MAILING NOTICE OF SPECIAL MEETING OF BOARD OF DIRECTORS

State of California
County of Los Angeles—ss.

J. C. Ballagh, being first duly sworn, deposes and says: That he is the duly appointed, qualified and acting Secretary of Patterson-Ballagh Corporation, a California corporation; that on the 18th day of August, 1939, he served copies of the following notice of a special meeting of the Board of Directors of said corporation upon each and every director by depositing in the United States mail, in a securely fastened, prepaid wrapper a true copy thereof, addressed to such Director of said corporation at his respective last known post office address as the same appears on the books and records of the corporation.

(Sgd) J. C. BALLAGH

Subscribed and sworn to before me this 18 day of August, 1939.

[Notarial Seal] (Sgd) MAY G. NOLAN
Notary Public in and for the County of Los Angeles, State of California.

"Los Angeles, Calif.
August 18, 1939

"A special meeting of the Board of Directors of Patterson-Ballagh Corporation will be held on

Plaintiff's Exhibit No. 1—(Continued)

Tuesday, August 22, 1939, at 11:00 o'clock a. m. at the office of the corporation, 1900 East 65th Street, Los Angeles, California.

Very truly yours,

J. C. BALLAGH

J. C. Ballagh

Secretary"

MINUTES OF ANNUAL MEETING OF SHAREHOLDERS OF PATTERSON-BALLAGH CORPORATION

The Annual Meeting of the Shareholders of Patterson-Ballagh Corporation, a California corporation, was held at the office and principal place of business of the company, located at 1900 East 65th Street, Los Angeles, California, on the 16th day of January, 1940, at the hour of 8:30 o'clock a.m., pursuant to notice issued.

Mr. D. G. Miller, President of the Corporation, presided at the meeting, and Mr. J. C. Ballagh, Secretary of the Corporation, acted as Secretary.

The Secretary presented and read the notice of the meeting, and it was ordered that a copy of same be placed in the minute book immediately following the minutes of this meeting.

The Secretary presented an affidavit, duly signed and sworn to by himself, showing that notice of the meeting had been mailed to each shareholder, addressed to such shareholder at the address given

Plaintiff's Exhibit No. 1—(Continued)

by him to the Corporation, postage prepaid. The affidavit was approved and ordered attached to these minutes.

The Secretary read the roll of the shareholders entitled to vote at the meeting, as follows:

Name	No. of Shares
Ballagh, J. C.	125
Byron Jackson Co., (a corporation) by E. S. Dulin, Pres.	249
Dulin, E. S.	1
Highland Investment Corp., Ltd. by J. C. Ballagh, Pres.	250
Miller, D. G. (voting stock of C. L. Patterson)	375
Total Capital Stock	1,000

Upon a call of the list it was found that there were present in person shareholders of the Corporation holding 750 shares of stock, as follows:

Name	No. of Shares
Ballagh, J. C.	125
Highland Investment Corp., Ltd. by J. C. Ballagh, Pres.	250
Miller, D. G. (voting stock of C. L. Patterson)	375
Total	750

The Secretary reported that the above number of shares represented more than a majority of the total number of shares outstanding and entitled to vote.

The Secretary then presented the minutes of the Annual Meeting of Shareholders held on January 27, 1939, which were read and approved.

Plaintiff's Exhibit No. 1—(Continued)

The financial report of the Corporation for the period ending November 30, 1939, as prepared under the direction of the Secretary-Treasurer, was presented and unanimously approved, and a summary of same was ordered attached hereto and made a part of the minutes of this meeting.

Upon motion duly made and seconded, it was unanimously

> Resolved, That the acts of Directors and Officers during the period since the last meeting of Shareholders be, and the same hereby are, fully ratified, approved, and confirmed.

The meeting then proceeded to the election of a Board of Directors for the ensuing year.

Upon motion duly made and seconded it was unanimously

> Resolved, That the present Directors be re-elected for the ensuing year, or until their successors are chosen and elected, which act can only be accomplished by the majority approval of the Shareholders.

No other business having come before the meeting, it was, on motion duly made and seconded, adjourned.

(Sgd) D. G. MILLER
President

(Sgd) J. C. BALLAGH
Secretary

Plaintiff's Exhibit No. 1—(Continued)

PATTERSON-BALLAGH CORPORATION

Secretary's Report of 1939 Operations to November 30, 1939

INCOME and PROFIT and LOSS

Gross Sales		$296,096.58
Cost of Goods Sold	$79,074.97	
Royalties	13,181.33	92,256.30
Gross Profit from Manufacturing		203.840.28
Operating Expenses		167,929.14
Net Income from Operations		35,911.14
Other Expenses—Less Other Income		11,563.22
Net Gain for period, before Income Tax Deduction		24,347.92
Less Estimated Federal & State Taxes		3,967.09
		20,380.83

Summary of Surplus

Balance as per Ledger November 30, 1938		$126,947.30
1939 Credits:		
Net Profit from Operations (before Federal & State Tax)		24,347.92
		151,295.22
1939 Charges:		
Federal Income Tax 1938	5,887.99	
Dividends		5,887.99
Total Earned Surplus at 11/30/39		145,407.23
Appreciated Surplus		1,611.86
Balance Surplus as per Ledger 11/30/39		147,019.09
Less Estimated Taxes for 1939		
Est. Federal Income Tax 1939	3,420.67	
Est. State Franchise Tax & Income	546.42	3,967.09
Surplus Balance after Estimated Taxes		143,052.00
Note: Estimated Federal Income Tax	3,420.67	
Est. State Franchise & Income Tax	546.42	
Total	3,967.09	for 1939 operations, payable during 1940. 1938 tax of $5,887.99 has been

Plaintiff's Exhibit No. 1—(Continued)

deducted to show surplus of $147,019.09, as shown on our books.

Item of $3,420.67 is chargeable against surplus in 1940, while item of $546.42 is chargeable against 1940 Profit and Loss.

For this reason Net Profit from Operations is shown before tax.

I, J. C. Ballagh, as Secretary-Treasurer of Patterson-Ballagh Corporation, hereby certify that the foregoing report is true, to the best of my knowledge and belief.

(Sgd) J. C. BALLAGH
J. C. Ballagh, Secretary-Treasurer

NOTICE OF ANNUAL MEETING OF SHAREHOLDERS OF PATTERSON-BALLAGH CORPORATION

Notice Is Hereby Given That the Annual Meeting of the Shareholders of Patterson-Ballagh Corporation, a California Corporation, Will Be Held on Tuesday, the 16th Day of January, 1940, at 8:30 o'clock A.M., at 1900 East 65th St., in the City of Los Angeles, County of Los Angeles, State of California, for the Following Purposes:

1.—To Receive and Consider a Report Covering the Business Activities of the Corporation During the Year Ending November 30, 1939.

2.—To Elect a Board of Directors to Serve Until the Next Annual Meeting of Shareholders.

3.—To Consider and Act Upon the Matter of Ratifying All Actions Taken by the Officers and Directors During the Period Since the Last Meeting of the Shareholders.

Plaintiff's Exhibit No. 1—(Continued)

4.—To Transact Such Other Business as May Properly Come Before the Meeting.

Dated this 5th day of January, 1940.

(Sgd) J. C. BALLAGH
J. C. Ballagh
Secretary

AFFIDAVIT OF MAILING NOTICE OF ANNUAL MEETING OF SHAREHOLDERS

State of California
County of Los Angeles—ss.

J. C. Ballagh, being first duly sworn, deposes and says: That he is the duly appointed, qualified and acting Secretary of Patterson-Ballagh Corporation, a California corporation; that on the 5th day of January, 1940, he served copies of notice of Annual Meeting of Shareholders of said corporation upon each and every shareholder by depositing in the United States mail, in a securely fastened, prepaid wrapper a true copy thereof, addressed to such shareholders of said corporation at their last known post office address as the same appears on the books and records of the corporation.

(Sgd) J. C. BALLAGH

Subscribed and sworn to before me this 5th day of January, 1940.

(Sgd) MAY G. NOLAN,
Notary Public in and for the County of Los Angeles, State of California.

Plaintiff's Exhibit No. 1—(Continued)

Los Angeles, California
January 5, 1940

The Annual Meeting of the Board of Directors of Patterson-Ballagh Corporation will be held on Tuesday, January 16, 1940, immediately following the Annual Meeting of Shareholders at 8:30 o'clock a.m., at the office of the corporation, 1900 East 65th Street, Los Angeles, California.

(Sgd) J. C. BALLAGH
J. C. Ballagh
Secretary

MINUTES OF ANNUAL MEETING OF DIRECTORS OF PATTERSON-BALLAGH CORPORATION

The annual meeting of the directors of Patterson-Ballagh Corporation was held at the office and principal place of business of the company, 1900 East 65th Street, Los Angeles, California, on the 16th day of January, 1940, immediately following the annual meeting of the shareholders.

Present:

J. C. Ballagh
D. G. Miller
H. C. Armington

Absent:

E. S. Dulin
Howard Burrell

Plaintiff's Exhibit No. 1—(Continued)

Mr. D. G. Miller, President of the Corporation, presided, and Mr. J. C. Ballagh acted as Secretary of the meeting.

The Secretary presented the notice of the meeting pursuant to which the meeting was held, which was approved and ordered attached to these minutes.

The Secretary then presented the minutes of the meeting of the Board of Directors held on August 22, 1939, which were read and approved.

The first business to come before the meeting was the election of officers for the ensuing year, and the following persons were nominated for the ensuing year for the respective offices, to-wit:

D. G. Miller, President
J. C. Ballagh, Secretary-Treasurer
M. G. Nolan, Asst. do

There being no further nominations, and the nominations of the above named persons being duly seconded, a vote was had and the Secretary declared the said persons unanimously elected for the said respective offices for the ensuing year.

Each of the officers so elected was present and thereupon accepted the office to which he was elected.

There being no further business to come before the meeting, the same was, upon motion, adjourned.

(Sgd) D. G. MILLER
President

(Sgd) J. C. BALLAGH
Secretary

Plaintiff's Exhibit No. 1—(Continued)

MINUTES OF SPECIAL MEETING OF BOARD OF DIRECTORS OF PATTERSON-BALLAGH CORPORATION

A special meeting of the Board of Directors of Patterson-Ballagh Corporation was held on the 18th day of March, 1940, at 1900 East 65th Street, Los Angeles, California, at the hour of 11:00 o'clock A. M. of said day, pursuant to notice duly and regularly given by the Secretary to each of the Directors, in accordance with the requirements of the By-Laws of the corporation.

Directors Present:

J. C. Ballagh
Howard Burrell
E. S. Dulin
D. G. Miller

Directors Absent:

H. C. Armington

Certificate of Secretary

The President called the meeting to order and presided thereover. The Secretary presented a certificate to the effect that due and regular notice of the meeting had been given to each of the Directors in accordance with the requirements of the By-Laws of the corporation. It was directed that the certificate be placed in the minute book immediately following the minutes of this meeting.

Plaintiff's Exhibit No. 1—(Continued)

Reading and Approval of Minutes

It was stated that the next order of business was the consideration of the minutes of the organization meeting of the Board of Directors held on the 16th day of January, 1940, immediately after the adjournment of the annual meeting of shareholders. The Secretary then presented the minutes of said meeting.

Thereupon, on motion of Director Dulin, seconded by Director Burrell and unanimously carried, it was

> Resolved, that the minutes of the organization meeting of the Board of Directors of this corporation held on the 16th day of January, 1940, shall be and the same are hereby approved as read.

Report of President

The President then presented a general report on the condition of the business and affairs of the corporation and the same indicated that the volume of business being enjoyed was considerably in excess of that experienced during the same period of the previous year and that earnings were expanding by reason thereof. He also reviewed certain economies that had been placed in effect in the offices of the corporation and advised the Directors of certain improvements being made in the plant, consisting of the renovation of the men's dressing room, the installation of a new lathe, presses, and certain other equipment. A general

Plaintiff's Exhibit No. 1—(Continued)

discussion of the report followed and the Directors expressed themselves as being gratified with the current condition of the business and affairs of the corporation.

Compensation of President

The meeting then proceeded with a discussion of the subject of increasing the compensation of the President to the extent of $500.00 a month, commencing as of the 1st day of March, 1940, at the suggestion of Director Ballagh. It was pointed out that under the administration of the President a number of economies had been effected and that the affairs of the corporation were being so operated as to materially enhance the net profit being derived from its activities, and further that the amount of earnings currently being experienced were more than sufficient to justify said increase. Director Dulin stated that he had no objection to making an increase in the compensation being paid to the President but expressed himself as feeling that the same should not be made for any definite period and with the understanding that it should not remain in effect beyond any reversal in the current trend of favorable business conditions.

Thereupon, on motion, duly seconded and carried, Director Miller not voting thereon, it was

Resolved, that the compensation being paid by this corporation to De Mont G. Miller, its President, for his services as such, shall be

Plaintiff's Exhibit No. 1—(Continued)

and the same is hereby increased as of March 1, 1940, from the sum of $1,000.00 per month to the sum of $1,500.00 per month, to continue until further action of this Board of Directors and with the understanding that the same may be decreased in the event of the appearance of a reversal in the current trend of favorable business conditions.

Compensation of Secretary-Treasurer

The President then suggested that the Directors consider the amount of compensation being paid by the corporation to Director Ballagh, as the Secretary-Treasurer thereof, and pointed out that his services in addition to those of said office also include those of a sales manager, in view of the fact that Director Ballagh was and had been for many years in complete charge of all sales activities of the corporation. The statement was made that during the last few months there had been sharp increase in the volume of sales and that the efforts devoted to the business of the corporation by Director Ballagh had been showing very satisfactory results. The suggestion was made that the monthly compensation being paid Director Ballagh be increased to the extent of $1,000.00 a month and that the quarterly compensation being paid to him remain the same. Director Dulin stated that he objected most strenuously to the suggested increase and expressed himself as feeling that the same was entirely unwarranted and should not be put into

Plaintiff's Exhibit No. 1—(Continued)

effect under any conditions until the corporation was paying satisfactory dividends to its shareholders.

Thereupon, on motion of Director Miller, seconded by Director Burrell and carried, Director Dulin voting in the negative and Director Ballagh not voting thereon, it was

> Resolved, that the monthly compensation being paid by this corporation to J. C. Ballagh, its Secretary and Treasurer, for his services as such and in the supervision of the sales activities of this corporation, shall be and the same is hereby increased as of March 1, 1940, from the sum of $1,000.00 per month to the sum of $2,000.00 per month, to continue until further action of this Board of Directors and with the understanding that the same may be decreased in the event of the appearance of a reversal in the current trend of favorable business conditions;
>
> Further Resolved, that the quarterly compensation being paid by this corporation to J. C. Ballagh, its Secretary and Treasurer, for his services as such and in the supervision of the sales activities of this corporation in the amount of $1,000.00 a quarter shall remain the same and shall not be deemed to have been changed or modified by the foregoing resolution.

Discussion of Dividend

There followed a discussion of the advisability of declaring and distributing a dividend on the

Plaintiff's Exhibit No. 1—(Continued)

outstanding shares of the capital stock of the corporation at this time and the suggestion was made that no such action should be taken until the amount of the earnings for the current year were more ascertainable and a clearer conclusion as to the effect of the international situation on the business of the corporation could be obtained. Director Dulin expressed himself as feeling that serious consideration should be given the matter of declaring a dividend at this time, but the concensus of opinion of the Directors was that the subject should be held in abeyance until later in the fiscal year.

Adjournment

There being no further business to come before the meeting, on motion, duly seconded and unanimously carried, the meeting was adjourned.

(Sgd) J. C. BALLAGH
Secretary

Approved:

(Sgd) D. G. MILLER
President

CERTIFICATE OF MAILING NOTICE OF SPECIAL MEETING OF THE BOARD OF DIRECTORS

J. C. Ballagh hereby certifies that he is the duly elected, qualified and acting Secretary of Patterson-Ballagh Corporation, a California corporation, and that on the 12th day of March, 1940, he served the

Plaintiff's Exhibit No. 1—(Continued)

following notice of a meeting of the Board of Directors of Patterson-Ballagh Corporation upon each and every Director of said corporation by depositing in the United States mail, in a securely fastened, prepaid wrapper, a true copy thereof, addressed to each and every Director of said corporation at their respective last known post office addresses as the same appear on the books of the corporation.

(Sgd) J. C. BALLAGH

"Los Angeles, California
March 12, 1940

"A special meeting of the Board of Directors of Patterson-Ballagh Corporation will be held on Monday, March 18, 1940, at 11:00 o'clock a. m. at the office of the corporation, 1900 East 65th Street, Los Angeles, California.

Very truly yours,
J. C. BALLAGH
J. C. Ballagh, Secretary"

MINUTES OF SPECIAL MEETING
OF BOARD OF DIRECTORS OF
PATTERSON-BALLAGH CORPORATION

A special meeting of the Board of Directors of Patterson-Ballagh Corporation was held on the 29th day of November, 1940, at 1900 East 65th Street, Los Angeles, California, at the hour of 9:00

Plaintiff's Exhibit No. 1—(Continued)

o'clock A. M. of said day, pursuant to notice duly and regularly given to each of the Directors in accordance with the requirements of the By-Laws of the corporation.

Directors Present:

H. C. Armington
J. C. Ballagh
Howard Burrell
D. G. Miller

Directors Absent:

E. S. Dulin

Certificate of Secretary

The President called the meeting to order and presided thereover. The Secretary presented a certificate to the effect that due and regular notice of the meeting had been given to each of the Directors in accordance with the By-Laws of the corporation. It was directed that the certificate be placed in the minute book immediately following the minutes of this meeting.

Absence of Director Dulin

The Secretary reported that he had been advised by Director Dulin that he would be unable to attend the meeting and that he hoped the same would be adjourned until the following week so that he could be in attendance. It was pointed out to the Directors that there were certain matters which should be completed before the end of the current fiscal year of the company on November 30, 1940, and it

Plaintiff's Exhibit No. 1—(Continued)

was agreed that only such matters would receive attention and that all other matters for consideration would be placed before the Board at an adjourned meeting when Director Dulin could be in attendance.

Reading and Approval of Minutes

The Directors then proceeded with the consideration of the minutes of the special meeting of the Board of Directors held on the 18th day of March, 1940, and the Secretary presented and read said minutes to the meeting.

Thereupon, on motion of Director Armington, seconded by Director Burrell and unanimously carried, it was

> Resolved, that the minutes of the special meeting of the Board of Directors of this corporation held on the 18th day of March, 1940, shall be and the same are hereby approved as read.

Bonus to Regular Employees

The President then suggested that the Directors consider the matter of the giving of a year-end bonus to the regular employees of the company, as had been the custom in the past. He stated that by the term "regular employees" he did not include R. A. McWaid, H. C. Armington, J. N. O'Melveny, J. C. Ballagh and himself, who were engaged in executive activity, and reported that it was his opinion that the year-end bonus to the regular employees should be in an amount equivalent to one-twelfth of

Plaintiff's Exhibit No. 1—(Continued)

the annual compensation actually received by them, less compensation received on account of over time. The Directors then discussed the suggested bonus and it was the consensus of their opinion that the same should be paid immediately and before the end of the current fiscal year.

Thereupon, on motion of Director Ballagh, seconded by Director Armington and unanimously carried, it was

> Resolved, that the proper officers of this corporation shall be and they are hereby authorized and directed to pay and deliver to its regular employees, other than R. A. McWaid, H. C. Armington, J. N. O'Melveny, J. C. Ballagh and D. G. Miller, immediately and prior to the end of the current fiscal year a year-end bonus to each thereof equivalent to one-twelfth of the compensation actually paid or to be paid by this corporation to each employee during the current fiscal year, less compensation received on account of over time, as a token of the appreciation of this corporation of the loyalty and services of its employees.

Year-End Bonus of R. A. McWaid and J. N. O'Melveny

The Directors then considered the matter of the payment of a year-end bonus to R. A. McWaid and J. N. O'Melveny, and the suggestion was made that such bonus should be in an amount equivalent to one-sixth of the compensation actually received and

Plaintiff's Exhibit No. 1—(Continued)

to be received by said persons from the company during the current fiscal year.

Thereupon, on motion of Director Armington, seconded by Director Burrell and unanimously carried, it was

Resolved, that the proper officers of this corporation shall be and they are hereby authorized and directed to pay and deliver to R. A. McWaid and J. N. O'Melveny immediately and prior to the end of the current fiscal year a year-end bonus to each thereof equivalent to one-sixth of the compensation actually paid or to be paid by this corporation to him during the current fiscal year, as a token of the appreciation of this corporation of his loyalty and service.

Additional Compensation to H. C. Armington

The Directors then proceeded with a consideration of the matter of the company paying H. C. Armington, a Director, additional compensation for his services rendered to it during the current fiscal year, and the President suggested that he be paid as such additional compensation an amount equivalent to one-sixth of the compensation actually received and to be received by him from the company during the current fiscal year. A discussion of the matter followed and the Directors expressed themselves as feeling that such an amount of additional compensation should be paid.

Thereupon, on motion, duly seconded and carried, Director Armington not voting thereon, it was

Resolved, that the proper officers of this cor-

Plaintiff's Exhibit No. 1—(Continued)

poration shall be and they are hereby authorized and directed to pay to H. C. Armington as additional compensation for his services rendered to the company during the fiscal year ending on November 30, 1940, a sum equivalent to one-sixth of his regular compensation paid or payable to him by this corporation for his services during the current fiscal year.

Additional Compensation to J. C. Ballagh

The President then suggested that the Directors consider the payment of additional compensation for the current fiscal year to Director Ballagh, and pointed out that he had been serving as the Secretary and Treasurer as well as the Sales Manager of the company and that due to his efforts the company had been enjoying an exceptionally fine volume of business and that its earnings were being materially increased, with excellent prospects for a further increase during the next fiscal year. Director Armington suggested that Director Ballagh be paid additional compensation for his services during the current fiscal year in an amount equivalent to one-sixth of his regular compensation paid or payable to him by the company for said year.

Thereupon, on motion of Director Armington, seconded by Director Burrell and carried, Director Ballagh not voting thereon, it was

Resolved, that the proper officers of this corporation shall be and they are hereby authorized and directed to pay to J. C. Ballagh as additional compensation for his services ren-

Plaintiff's Exhibit No. 1—(Continued)

dered to the company during the fiscal year ending on November 30, 1940, a sum equivalent to one-sixth of his regular compensation paid or payable to him by this corporation for his services during the current fiscal year.

Additional Compensation to D. G. Miller

The subject of paying additional compensation to Director Miller, the President of the corporation, was then brought up for discussion and the extent and value of his services rendered during the current fiscal year were reviewed in detail. After a consideration of said services the suggestion was made that he should be additionally compensated by the company therefor to the same extent as other executives in that his services were of a comparable value.

Thereupon, on motion of Director Ballagh, seconded by Director Armington and carried, Director Miller not voting thereon, it was

Resolved, that the proper officers of this corporation shall be and they are hereby authorized and directed to pay to D. G. Miller as additional compensation for his services rendered to the company during the fiscal year ending on November 30, 1940, a sum equivalent to one-sixth of his regular compensation paid or payable to him by this corporation for his services during the current fiscal year.

Adjournment

At this point the Directors agreed that there were

Plaintiff's Exhibit No. 1—(Continued)

no other matters that required decision before the end of the current fiscal year of the company on November 30, 1940, and on motion, duly seconded and unanimously carried, the meeting was adjourned until December 3, 1940, at the hour of 9:00 o'clock A. M. so as to permit the attendance of Director Dulin during the balance of the meeting.

(sgd) J. C. BALLAGH
Secretary

Approved:

(Sgd) D. G. MILLER
President.

CERTIFICATE OF MAILING NOTICE OF SPECIAL MEETING OF THE BOARD OF DIRECTORS

J. C. Ballagh hereby certifies that he is the duly elected, qualified and acting Secretary of Patterson-Ballagh Corporation, a California corporation, and that on the 25th day of November, 1940, he served the following notice of a meeting of the Board of Directors of Patterson-Ballagh Corporation upon each and every Director of said corporation by depositing in the United States mail, in a securely fastened, prepaid wrapper, a true copy thereof, addressed to each and every Director of said corporation at their respective last known post office addresses as the same appear on the books of the corporation.

(Sgd) J. C. BALLAGH

Plaintiff's Exhibit No. 1—(Continued)

"Los Angeles, Calif.
November 25, 1940

Dear Sir:

A special meeting of the Board of Directors of Patterson-Ballagh Corporation will be held on Friday, November 29, 1940, at 9:00 a.m. at the office of the corporation, 1900 East 65th Street, Los Angeles, California.

Very truly yours,
J. C. BALLAGH
J. O. Ballagh, Secretary"

MINUTES OF ADJOURNED MEETING OF BOARD OF DIRECTORS OF PATTERSON-BALLAGH CORPORATION

An adjourned meeting of the Board of Directors of Patterson-Ballagh Corporation was held on the 3rd day of December, 1940, at 1900 East 65th Street, Los Angeles, California, at the hour of 9:00 o'clock A. M. of said day, pursuant to a resolution duly and regularly adopted by the Board of Directors at a special meeting held on the 29th day of November, 1940.

Directors Present:
H. C. Armington
J. C. Ballagh
Howard Burrell
E. S. Dulin
D. G. Miller

Directors Absent:
None

Plaintiff's Exhibit No. 1—(Continued)

The President called the meeting to order and presided thereover.

Financial Statement

There was presented to the meeting a statement prepared by the accounting department of the company containing a balance sheet indicating the financial condition at October 31, 1940, and an operating statement showing results of operations during the month of October and during the first eleven months of the fiscal year ending on November 30, 1940. The contents of the statement were discussed at length and no action was taken in respect thereto.

The suggestion was made that a reserve be maintained to cover contingent liabilities of the company, in respect to taxes and possible requirements for the payment of royalties on certain of its products, and it was the consensus of opinion of the Directors that this should be done.

Payment of Dividend

Director Dulin suggested that the Directors consider the matter of the declaration and payment of a dividend on the issued and outstanding shares of the capital stock of the company and stated that in view of the additional compensation being paid by the company to its officers and Directors, which he considered more than adequate, it appeared that the company was in a position to declare and pay a dividend to its shareholders. Directors Miller and Ballagh stated that they were of the opinion that

Plaintiff's Exhibit No. 1—(Continued)

no action should be taken in respect to dividends at this time in view of the cash requirements of the company under a proposal to be presented for the expansion of its plant facilities and in view of pending litigation involving the question as to the requirement of paying royalties on protectors manufactured and sold and the validity of the patents on its manual and hydraulic applicators. A further discussion of the matter of the declaration and payment of the dividend followed but no action was taken thereon.

Acquisition of Real Property and Improvement Thereof

The President then presented to the meeting a proposal contemplating the acquisition by the company of additional real property with improvements thereon consisting of an old residence, or residences, lying immediately south of the plant of the company, and upon the acquisition thereof to clear said property and erect thereon a warehouse or other buildings for the storage of carbon black, rubber and other supplies. He stated that in his opinion the property could be acquired and the proposed improvements placed thereon at a cost of not to exceed $5,000.00 in amount.

There followed a discussion of the proposal and it was the thought of the Directors that said program should be followed and that the possibility of acquiring an additional fifty feet of property to

Plaintiff's Exhibit No. 1—(Continued)

that contained in the proposal of the President be explored and reported to the Directors at the next meeting.

Thereupon, on motion of Director Dulin, seconded by Director Burrell and unanimously carried, it was

Resolved, that the proper officers of this corporation shall be and they are hereby authorized to acquire for and on behalf of this corporation the real property located immediately south of its plant and described at this meeting and to erect thereon a warehouse or other buildings for the storage of carbon black, rubber and other supplies at a total cost of not to exceed $5,000.00 in amount;

Further Resolved, that the proper officers of this corporation shall be and they are hereby authorized and directed to explore the possibility of the acquisition by this company of an additional fifty feet of property located south of the parcels hereinbefore authorized to be purchased and report thereon at the next meeting of the Board of Directors.

Expansion of Plant Facilities

There was then discussed generally by the Directors the suggestion of the President and Secretary that the company consider the advisability of improving its property across the street to the east of its plant by the erection of a building to house the present machine shop and such additional machine tools as might be acquired, and the acquisition

Plaintiff's Exhibit No. 1—(Continued)

of equipment to be placed therein for experimental work and development of new items to be manufactured and sold in the field of rubber and plastics as well as articles for use in the petroleum industry. The estimate was given that the proposed improvements would cost approximately $15,000.00 in amount and that probably the sum of $25,000.00 should be expended in new equipment, tools and laboratory. A general discussion followed but no action was taken in respect to the suggestion.

Investment of Funds

The President then offered the suggestion that the Directors consider the advisability of investing certain cash resources of the company in government securities so as to procure a higher return thereon than could be received from keeping the same in savings accounts. Directors Dulin and Burrell pointed out that in their opinion the return on government securities was now so low as not to justify the investment therein when the risk of depreciation in value was considered, and after a discussion of the subject it was decided that no action should be taken in respect thereto at this time.

"Idea-Dollar" Plan

The Secretary then presented a plan designated as "Idea-Dollar" plan for the making of awards to employees for suggestions in respect to the improvement of the operations of the company, the effecting of economies, and the development of its relations with its customers and the public. He

Plaintiff's Exhibit No. 1—(Continued)

handed the Directors for study a manual covering the details of the plan and reported that the cost of putting it into effect would probably be only nominal and not exceed the amount of $1,000.00 per year. A general discussion of the plan followed and it was the concensus of opinion of the Directors that the plan should be put into effect as of December 1, 1940, and continued for a period of six months and then reviewed.

Thereupon, on motion of Director Dulin, seconded by Director Ballagh and unanimously carried, it was

> Resolved, that the "Idea-Dollar" plan presented to this meeting by the Secretary shall be and the same is hereby adopted and put into effect as of December 1, 1940, for a period of six months and that the officers of this corporation shall be and they are hereby authorized to expend such funds of the corporation, not to exceed, however, $500.00 in amount, as may be necessary to carry out said plan during said period.
>
> Further Resolved, that at the expiration of six months the plan be reviewed and after a consideration of the results obtained thereunder further consideration be given to the matter of continuing it after the expiration of said period.

Adjournment

There being no further business to come before

Plaintiff's Exhibit No. 1—(Continued)

the meeting, on motion, duly seconded and unanimously carried, the meeting was adjourned.

(Sgd) J. C. BALLAGH
Secretary

Approved:

(Sgd) D. G. MILLER
President

CERTIFICATE OF MAILING NOTICE OF SPECIAL MEETING OF THE BOARD OF DIRECTORS

J. C. Ballagh hereby certifies that he is the duly elected, qualified and acting Secretary of Patterson-Ballagh Corporation, a California corporation, and that on the 25th day of November, 1940, he served the following notice of a meeting of the Board of Directors of Patterson-Ballagh Corporation upon each and every Director of said corporation by depositing in the United States mail, in a securely fastened, prepaid wrapper, a true copy thereof, addressed to each and every Director of said corporation at their respective last known post office addresses as the same appear on the books of the corporation.

(Sgd) J. C. BALLAGH

Plaintiff's Exhibit No. 1—(Continued)

"Los Angeles, California
November 25, 1940

"A special meeting of the Board of Directors of Patterson-Ballagh Corporation will be held on Friday, November 29, 1940, at 9:00 a. m. at the office of the corporation, 1900 East 65th Street, Los Angeles, California.

Very truly yours,
J. C. BALLAGH
J. C. Ballagh, Secretary"

MINUTES OF ANNUAL MEETING OF SHAREHOLDERS OF PATTERSON-BALLAGH CORPORATION

The annual meeting of shareholders of Patterson-Ballagh Corporation was held on Tuesday, the 21st day of January, 1941, at the hour of 8:30 o'clock A. M. of said day at the office and principal place of business of the corporation at 1900 East 65th Street, in the City of Los Angeles, County of Los Angeles, State of California, pursuant to notice of said meeting duly had and regularly given to all of the shareholders of record, in accordance with the By-Laws of the corporation.

The President called the meeting to order and presided thereover. He presented the affidavit of the Secretary to the effect that due and regular notice of the meeting had been given and it was di-

Plaintiff's Exhibit No. 1—(Continued)

rected that said affidavit be inserted in the minute book of the corporation immediately following the minutes of this meeting.

The President then requested the Secretary to call the roll and examine the proxies at hand to ascertain whether or not there were represented at the meeting in person or by proxy the holders of a majority of the subscribed, issued and outstanding shares of the capital stock of the corporation so as to constitute a quorum.

The Secretary called the roll and examined the proxies at hand and then reported the following shareholders present at the meeting:

Present in person:

Name of Shareholder	No. of Shares
J. C. Ballagh	125
E. S. Dulin	1

Present by Proxy:

Name of Shareholder	Name of Proxy	No. of Shares
Byron Jackson Co.	E. S. Dulin	249
Highland Investment Corp., Ltd.	J. C. Ballagh	250
C. L. Patterson	D. C. Miller	375

The President then declared that a total of 1,000 shares, being all of the subscribed, issued and outstanding capital stock of the corporation, were represented by the holders thereof being present in person or by proxy and that the meeting was therefore competent to proceed with the transaction of business.

Plaintiff's Exhibit No. 1—(Continued)

Reading and Approval of Minutes

It was announced that the next business before the meeting was a consideration of the minutes of the annual meeting of the shareholders held on the 16th day of January, 1940. The Secretary then presented the minutes of said meeting and there being no errors or omissions noted therein the same were approved as read.

Financial Statement

The President presented to the shareholders for consideration a tentative financial statement indicating the condition of the company at the close of its fiscal year on November 30, 1940, and the results of its operations during said fiscal year. The statement indicated that the company had earned approximately $51,586.00 during the year before federal income and state franchise taxes. The shareholders were advised that an audit covering the activities of the company during said fiscal year was being made and that the same would be completed within a short time and then made available to all of the shareholders for study and consideration.

Nomination of Directors

The meeting then proceeded with the nomination of persons to serve as Directors during the ensuing year or until the election or appointment of their successors, and J. C. Ballagh placed the names

Plaintiff's Exhibit No. 1—(Continued)

of H. C. Armington, J. C. Ballagh, Howard Burrell, E. S. Dulin and D. G. Miller in nomination.

Election of Directors

There being no further nominations, on motion of J. C. Ballagh, seconded by E. S. Dulin and unanimously carried, it was

> Resolved, that the nominations be closed and that the Secretary be instructed to cast a ballot on behalf of all shareholders present in person or by proxy for and in favor of the persons nominated as the Directors of this corporation.

The Secretary thereupon cast said ballot and announced that each of the five persons nominated had received 1,000 votes, and the President declared said nominees to be the duly elected Directors of the corporation for the ensuing year or until the election or appointment of their successors.

Ratification of Prior Acts of Officers and Directors

Thereupon, on motion of J. C. Ballagh, seconded by D. G. Miller and carried, E. S. Dulin voting in the negative, it was

> Resolved, that all action taken by the Board of Directors of this corporation since the date of the last annual meeting of the shareholders, whether said Directors were defacto or de jure, and all action of the officers of this corporation done pursuant to the authorization of the Board of Directors.

Plaintiff's Exhibit No. 1—(Continued)

or with the knowledge and acquiescence of the Directors are hereby ratified, approved and confirmed as and for the corporate acts of this corporation.

E. S. Dulin explained his vote in the negative on the foregoing resolution by stating that in his opinion the acts of the officers and Directors in accepting and fixing the amount of compensation paid during the last fiscal year to the President and Secretary was contrary to the best interests of the minority shareholders.

Adjournment

There being no further business to come before the meeting, on motion, duly seconded and unanimously carried, the meeting was adjourned.

(Sgd) J. C. BALLAGH,
Secretary.

Approved:

(Sgd) D. G. MILLER,
President.

CERTIFICATE OF MAILING NOTICE OF ANNUAL MEETING OF SHAREHOLDERS

J. C. Ballagh hereby certifies that he is the duly appointed and acting Secretary of Patterson-Ballagh Corporation, a California corporation, and that on the 11th day of January, 1941, he served the attached notice of the annual meeting of the shareholders of Patterson-Ballagh Corporation

Plaintiff's Exhibit No. 1—(Continued)

upon each and every shareholder of said corporation by depositing in the United States mail, in a securely fastened, prepaid wrapper, a true copy thereof addressed to each and every shareholder of said corporation at their respective last known postoffice addresses as the same appear on the books of the corporation.

(Sgd) J. C. BALLAGH,
Secretary of Patterson-Ballagh Corporation.

NOTICE OF ANNUAL MEETING OF PATTERSON-BALLAGH CORPORATION

Notice Is Hereby Given that the annual meeting of the shareholders of Patterson-Ballagh Corporation, a California corporation, will be held on Tuesday, the 21st day of January, 1941 ,at 8:30 o'clock A. M., at 1900 East 65th Street, in the City of Los Angeles, County of Los Angeles, State of California, for the following purposes:

1. To receive and consider the annual report covering the activities of the corporation during the calendar year ending December 31, 1940;

2. To elect a Board of Directors for the ensuing year;

3. To consider and act upon the matter of ratifying all action taken by the officers and directors during the period since the last meeting of the shareholders;

Plaintiff's Exhibit No. 1—(Continued)

4. To transact such other business as may properly come before the meeting.

Dated this 11th day of January, 1941.

J. C. BALLAGH,
Secretary.

MINUTES OF ORGANIZATION MEETING OF BOARD OF DIRECTORS OF PATTERSON-BALLAGH CORPORATION

An organization meeting of the Board of Directors of Patterson-Ballagh Corporation was held on the 21st day of January, 1941, at the hour of 9:00 o'clock A. M. of said day at the office and principal place of business of the corporation at 1900 East 65th Street, in the City of Los Angeles, County of Los Angeles, State of California, immediately following the adjournment of the annual meeting of shareholders, in accordance with the provisions of the By-Laws of the corporation.

Directors Present:

H. C. Armington
J. C. Ballagh
Howard Burrell
E. S. Dulin
D. G. Miller

Directors absent:

None.

Plaintiff's Exhibit No. 1—(Continued)

Appointment of Temporary Officers

On motion, duly seconded and unanimously carried, D. G. Miller was appointed as temporary Chairman and J. C. Ballagh as temporary Secretary of the meeting and they discharged their respective duties until the election of their successors.

Reading and Approval of Minutes

The Chairman announced that the first business before the meeting was a consideration of the minutes of the special meeting of the Board of Directors held on the 29th day of November, 1940, and of the adjourned meeting of the Board of Directors held on the 3rd day of December, 1940. The Secretary then presented the minutes of said meeting.

Thereupon, on motion of Director Armington, seconded by Director Burrell and carried, Director Dulin voting in the negative as to the minutes of the special meeting of the Board of Directors held on the 29th day of November, 1940, and in the affirmative as to the minutes of the adjourned meeting of the Board of Directors held on the 3rd day of December, 1940, it was

> Resolved, that the minutes of the special meeting of the *special meeting of the* Board of Directors held on the 29th day of November, 1940, and of the adjourned meeting of the Board of Directors held on the 3rd day of December, 1940, shall be and the same are hereby approved as read.

Plaintiff's Exhibit No. 1—(Continued)

Director Dulin explained his vote in the negative insofar as the minutes of the special meeting of the Board of Directors held on November 29, 1940, were concerned by stating that he was not in attendance at said meeting and therefore not familiar as to whether the minutes correctly reflected the action therein taken.

Nomination and Election of Officers

The meeting was then advised that the next order of business was the nomination and election of persons to serve as the officers of the corporation during the ensuing year, and Director Armington nominated the following persons for the offices set opposite their respective names:

President	D. G. Miller
Secretary	J. C. Ballagh
Treasurer	J. C. Ballagh
Assistant-Secretary	M. G. Nolan
Assistant-Treasurer	M. G. Nolan

There being no further nominations, on motion of Director Armington, seconded by Director Burrell and unanimously carried, it was

Resolved, that the nominations be closed and that the persons nominated as the officers of this corporation for the ensuing year shall be and they are hereby elected and appointed as such by acclamation.

Plaintiff's Exhibit No. 1—(Continued)

Report of President

The President reported to the Directors that the litigation commenced by the company in Oklahoma involving the validity of its patents covering the applicators or expanders of the company had been recently successfully terminated and that the litigation commenced against the company and certain of its officers and Directors by Byron Jackson Co. was still pending. The President also reported that the company had completed the acquisition at a cost of $2,200.00 of the real property authorized to be purchased by the Board of Directors at their adjourned meeting on December 3, 1940, but that he had not as yet been able to get a price on the additional fifty feet located immediately south of the land purchased.

Compensation of Officers

The suggestion was made that the Directors consider the advisability of working out a basis for the compensation of the President and Secretary of the corporation depending on the amount of the earnings resulting from its business operations, but in view of the fact that Director Dulin was required to leave the meeting for another engagement it was decided to put the matter over until the next meeting of the Board of Directors for further discussion and action.

Plaintiff's Exhibit No. 1—(Continued)

Adjournment

There being no further business to come before the meeting, on motion, duly seconded and unanimously carried, it was adjourned.

(Sgd) J. C. BALLAGH,
Secretary.

Approved:

(Sgd) D. G. MILLER,
President.

[Endorsed]: Filed 7/2/1942.

Mr. Lamont: The next minutes I refer to are the minutes of the meeting of June 20, 1938, and I am reading this simply to show that the other persons of that organization were paid comparatively small salaries. In other words, the money was all taken out by the executives, for a while by Patterson, and then by Miller.

"Resolved, That the salary of Mr. J. M. O'Melveny", who was, I think, the man in charge in the Middle West, "be increased from $354 to $375, effective July 1, 1938.

"Resolved Further, That Mr. O'Melveny be given a bonus of $25 when sales in the Mid-Continent area (comprising the states of Texas, Louisiana, Oklahoma, Arkansas, New Mexico, and Illinois) exceed $15,000 in any one month; $50 when the sales exceed $18,000, and $75 when

the sales exceed $21,000. This will in no way affect any yearly bonus which may be [13] paid by the corporation;

"Resolved Further, That the salary of Mr. T. M. Smith, Jr., be increased from $160 to $170 per month, effective July 1, 1938;

"Resolved Further, That a dividend of 6 per cent of the capital stock be paid out of the profits of the corporation, earned prior to June 30, 1938, to the stockholders on record as of June 30, 1938."

I simply quoted that to show that, outside of the two chief executives, the salaries were moderate. This shows the comparison between the salaries to those men and the salaries of the other people in the corporation.

The next I will read is for January 27, 1939, just before Mr. Miller came in. We are making no pretense in this case but what these executives are entitled to $1,000 a month. We have never complained of their management. We are complaining that they valued their services much too highly for the services they were rendering. As a matter of fact, Mr. Dulin voted to continue them as officers and also directors. There is no denial of that at all. And, after all, they were in control and he didn't have very much of a say on that. But as to their salaries I will show by letters from the parties that it was constantly objected to. And this resolution was presented by Mr. Dulin:

"Resolved, that the officers' salaries, viz: [14] Mr. Patterson and Mr. Ballagh, be each One

Thousand ($1,000.00) Dollars per month, effective January 1, 1939.

"Resolved, that all company correspondence shall be placed in the company files."

That is not important. That is simply brought out for that one reason.

At the meeting of February 15, 1939, I believe, Mr. Miller became a director, and we had no complaint in regard to him becoming a director. There had been a certain amount of contention between Mr. Patterson and Mr. Ballagh. However, from then on the trouble started. At the time he was elected, Mr. Armington was an employee of the company, on a very minor salary, and was also made a director at the suggestion of Mr. Miller and Mr. Ballagh. On June 29th, Mr. Burrell, who represented both Mr. Miller and——

Mr. Bednar: These statements are fine, but it seems to me if you confine yourself to the——

Mr. Lamont: I think we stipulated to all these things.

Mr. Bednar: There are some variations as you go along.

Mr. Lamont: I will proceed with the minutes, then. There is no doubt that on February 15, 1939, Mr. Miller was made a director, and also Mr. Armington.

Mr. Bednar: Mr. Miller was.

Mr. Lamont: And Mr. Armington also. On June 27, 1939, Mr. Burrell, as shown by the minutes—that was a very [15] short time after Mr. Miller came

into the organization—Byron Jackson was served with a notice which involved the repudiation of the patent agreement we had with them, which reads as follows. Before I come to that I had better present the minutes that were shown to the board. There was apparently a report by Mr. Miller, dated June 27, 1939, to the board of directors of the Patterson-Ballagh Corporation:

"Board of Directors
"Patterson-Ballagh Corporation
"Los Angeles, California

"Gentlemen:

"Since assuming office as President of Patterson-Ballagh Corporation I have taken upon myself the duty of studying the various costs in connection with the conduct of this business. I find that for the first six months of 1939 the corporation will show a loss of some $2,000. In this study of the various costs I noted the fact that the payment to Byron Jackson Company of royalties under the license agreement was a very substantial sum, and much more than made up the differences between profit and loss to the corporation.

"A study of the situation shows that the Bettis patent has been invalidated, and we are no longer operating thereunder. We have, however, been paying royalties to Byron Jackson [16] Company on the protectors, although we have not had any protection or benefit which would flow from a patent. Substantially all of our competitors on the other hand are not under the burden of paying royal-

ties. The payment of these royalties on an unpatented product has been an important factor in the sale of protectors, particularly in the export trade. As stated, these royalty payments mean the difference between operating at a profit or a loss, and it may ultimately drive us out of the export trade.

"The facts show that our sales of Patterson-Ballagh protectors to be used in connection with the so-called Hapkins cushion joint have been so small as not to warrant the time and expense involved, and because it has been assumed that the payment of royalties on the unpatented protectors is tied into the license agreement, the result has been a continuous loss.

"Because of all this, I asked the firm of Musick and Burrell to make a study of the situation to see if there was not some means by which payment under this agreement could be eliminated. They made an analysis of the situation and prepared a memorandum which is being [17] presented at this meeting. As a result of this analysis and this memorandum, I asked the Secretary to send out notice calling a meeting of the Board of Directors in order to consider this matter at greater length.

"Very truly yours,

"D. G. MILLER."

Then follows the opinion of Musick and Burrell. That all came along in June of 1939. Then the minutes will show that in August, 1939, not very long after this letter was written and presented to

the board, and irrespective of the supposed condition of the company, Mr. Ballagh's salary was increased to the extent of $4,000 as of March 1, 1939.

Mr. Bednar: It began about June 1, 1939.

Mr. Lamont: What I am emphasizing here is that Mr. Miller puts himself in writing to the effect that the company is in bad shape on June 27th, and then on August 27th he raises Mr. Ballagh's salary to the tune of $4,000 per year. And the same thing continues. In November, 1940, bonuses were declared, which amounted in each case—and the minutes show that—to one-sixth of their annual compensation.

Mr. Bednar: When was this?

Mr. Lamont: November 29, 1940.

Mr. Bednar: That is over a year and a half later.

Mr. Lamont: Thank you. I skipped something. [18]

On March 18, 1940, there was an additional raise to Ballagh of $1,000 per month, and then in November of 1940 there was this last raise of one-sixth of their salaries, which brought, as I have stated to the court, the total payment in 1940—and the minutes show it—to practically $15,000, and in 1941, up to September 10th, to the extent of $26,500, which I think at the end of the year was increased, so that the two parties—in other words that brings it up to $50,000.

Mr. Bednar: I didn't check the figure, but I believe that should be brought out by evidence and not by argument.

Mr. Lamont: It is all in the minutes. Now, in the depositions there is a salaries and bonus account. I ask that that be submitted in evidence, the transcript of it. It extends over several pages. I don't think on this phase of the case there will be very much argument, your Honor. May it be stipulated that there is an error here in this compilation? The date 12/16/39 should be 12/16/38.

Mr. Bednar: That is correct.

Mr. Lamont: That will be Plaintiff's Exhibit 2.

The Clerk: Plaintiff's Exhibit 2. This was supplied by counsel.

PLAINTIFF'S EXHIBIT No. 2

Plaintiff's Exhibit 10-a

D.C.S.D.Cal.Cent.Div.—Civ. #1763-Y.

Byron Jackson Co., Plff. v. Patterson-Ballagh Corp. et al., Dfts.

[Seal] MEYER WEISMAN
Notary Public

SALARIES—1938

Date	Ck.	J. C. B.	C. L. P.
1/14/38	152		500.00
"	153	500.00	
1/31/38	256		500.00
"	257	500.00	
2/15/38	388		500.00
"	387	500.00	
2/28/38	446		500.00
"	447	500.00	
3/16/38	537		500.00
"	538	500.00	
3/31/38	664		500.00
"	665	500.00	
4/15/38	766		500.00
"	767	500.00	

Salaries—1938—(Continued)

Date	Ck.	J. C. B.	C. L. P.
4/30/38	755		500.00
"	756	500.00	
5/17/38	997		500.00
"	996	500.00	
5/31/38	1097		500.00
"	1098	500.00	
6/15/38	1233		500.00
"	1234	500.00	
6/30/38	1337		500.00
"	1338	500.00	
7/15/38	1452		500.00
"	1453	500.00	
7/31/38	1536		500.00
"	1537	500.00	
8/15/38	1670		500.00
"	1671	500.00	
8/31/38	1743		500.00
"	1744	500.00	
9/15/38	1894		500.00
"	1895	500.00	
9/30/38	1957		500.00
"	1958	500.00	
10/15/38	2101		500.00
"	2102	500.00	
10/31/38	2175		1500.00
"	2176	1500.00	
11/16/38	2311		750.00
"	2312	750.00	
11/30/38	2381		750.00
"	2380	750.00	
		$12500.00	$12500.00

Plaintiff's Exhibit 10-b & 10-c (including last two items on original penciled sheet submitted by defendants, previously marked Ex. 10-c).

D.C.S.D. Cal. Cent. Div.—Civ. #1762-Y.

Byron Jackson Co., Plff. v. Patterson-Ballagh Corp. et al., Dfts.

Plaintiff's Exhibits 10-b & 10-c (one sheet—consolidated from two original penciled sheets.)

[Seal] MEYER WEISMAN
Notary Public

SALARIES—1939

Date	Ck.	J. C. B.	C. L. P.	D. G. M.
12/16/38	102		750.00	
"	103	750.00		
12/31/38	156		750.00	
"	157	750.00		
1/16/39	303		750.00	
"	304	750.00		
1/30/39	375		250.00	
"	376	250.00		
2/15/39	499		535.75	
"	501	500.00		
2/28/39	562			464.29
"	563	500.00		
3/15/39	676			500.00
"	677	500.00		
3/31/39	744			500.00
"	745	500.00		
4/13/39	815			500.00
"	816	500.00		
4/28/39	928			500.00
"	929	500.00		
5/15/39	1058			500.00
"	1059	500.00		
5/31/39	1108			500.00
"	1109	500.00		
5/31/39	1115	1000.00		
6/15/39	1151			500.00
"	1152	500.00		
6/30/39	1276			500.00
"	1277	500.00		
7/14/39	1308			500.00
"	1309	500.00		
7/31/39	1450			500.00
"	1451	500.00		

Salaries—1939—(Continued)

Date	Ck.	J. C. B.	C. L. P.	D. G. M.
8/15/39	1497			500.00
"	1498	500.00		
8/31/39	1631			500.00
8/28/39	1619	1500.00		
9/15/39	1668			500.00
"	1669	500.00		
9/29/39	1742			500.00
"	1743	500.00		500.00
10/13/39	1792			500.00
"	1793	500.00		
10/31/39	1948			500.00
"	1949	500.00		
11/15/39	1982			500.00
"	1983	500.00		
11/29/39	2104			500.00
"	2105	1500.00		
		$15500.00	$3035.71	$9464.29

Plaintiff's Exhibit 10-d

D.C.S.D. Cal. Cent. Div.—Civ. #1762-Y.

Byron Jackson Co., Plff. v. Patterson-Ballagh Corp, et al., Dfts.

Plaintiff's Exhibit 10-d.

[Seal] MEYER WEISMAN
Notary Publie

SALARIES—1940

Date	Ck.	J. C. B.	D. G. M.
12/15/39	2169		500.00
"	2170	500.00	
12/29/39	2258		500.00
"	2259	500.00	
1/15/40	2301		500.00
"	2302	500.00	
1/31/40	2398		500.00
"	2399	500.00	
2/13/40	2438		500.00
"	2439	1500.00	

Salaries—1940—(Continued)

Date	Ck.	J. C. B.	D. G. M.
2/29/40	2545		500.00
2/23/40	2529	500.00	
3/15/40	2583		500.00
"	2584	500.00	
3/18/40	2601		250.00
"	2600	500.00	
3/30/40	2702		250.00
"	2703	500.00	
3/29/40	2699		500.00
"	2700	500.00	
4/15/40	2802		750.00
"	2803	1000.00	
4/30/40	2856		750.00
4/23/40	2843	1000.00	
5/14/40	2965		750.00
"	2966	1000.00	
5/28/40	52	2000.00	
5/28/40	53		750.00
6/13/40	156		750.00
"	158	1000.00	
6/28/40	197		750.00
"	198	1000.00	
7/15/40	275		750.00
"	276	1000.00	
7/31/40	313		750.00
"	314	1000.00	
8/15/40	429		750.00
"	428	1000.00	
8/19/40	435	1000.00	
8/29/40	463		750.00
8/30/40	472	1000.00	
9/10/40	583		750.00
"	584	1000.00	
9/30/40	634		750.00
"	635	1000.00	
10/14/40	715		750.00
"	716	1000.00	

Plaintiff's Exhibit 10-e

D.C.S.D.Cal.Cent.Div.—Civ. #1762-Y.
Byron Jackson Co., Plff. v. Patterson-Ballagh Corp. et al., Dfts.
Plaintiff's Exhibit 10-e.

[Seal] MEYER WEISMAN
Notary Public.

SALARIES—1940

Date	Ck.	J. C. B.	D. G. M.
10/31/40	743		750.00
"	744	1000.00	
11/15/40	837		750.00
"	838	1000.00	
11/27/40	864	1000.00	
11/29/40	868	1000.00	
"	869		750.00
11/29/40	871		2750.00
"	872	4166.66	
		29166.66	19250.00

Plaintiff's Exhibit 10-f

D.C.S.D.Cal.Cent.Div.—Civ. #1762-Y
Byron Jackson Co., Plff. v. Patterson-Ballagh Corp. et al., Dfts.
Plaintiff's Exhibit 10f.

[Seal] MEYER WEISMAN
Notary Public.

SALARIES—1941

Date	Ck.	J. C. B.	D. G. M.
12/13/40	971	1000.00	
"	970		750.00
12/31/40	1023	1000.00	
"	1024		750.00
1/15/41	1100		750.00
"	1099	1000.00	
1/31/41	1147	1000.00	
"	1148		750.00
2/14/41	1216	1000.00	
"	1217		750.00
"	1219	1000.00	

Plaintiff's Exhibit No. 2—(Continued)

Salaries—1941—(Continued)

Date	Ck.	J. C. B.	D. G. M.
2/28/41	1249	1000.00	
"	1251		750.00
3/14/41	1327	1000.00	
"	1328		750.00
3/31/41	1371	1000.00	
"	1372		750.00
4/14/41	1470	1000.00	
"	1471		750.00
4/30/41	1497		750.00
/	1498	1000.00	
5/15/41	1592	1000.00	
"	1593		750.00
5/28/41	1634	1000.00	
5/29/41	1636	1000.00	
"	1637		750.00
6/13/41	1730	1000.00	
"	1731		750.00
6/30/41	1784	1000.00	
"	1786		750.00
7/15/41	1885	1000.00	
"	1886		750.00
7/31/41	1947		750.00
"	1948	1000.00	
8/15/41	2037		750.00
"	2038	1000.00	
8/29/41	2127	1000.00	
"	2128		750.00
8/29/41	2130	1000.00	
		2100.00	13500.00

[Endorsed]: Filed Jun 29 1942. Edmund L. Smith, Clerk.

[Endorsed]: Filed July 2, 1942 by Cross, Dep. Clerk.

Mr. Bednar: May I make a suggestion at this point? That last exhibit is made up of the dates and check numbers and amounts of the checks, and it is compiled on the basis of the fiscal year of the corporation, which runs from [19] December 1 to December 1, and the resolutions in the minutes provided for compensation on the basis of the calendar year, so that there has to be a reconciliation of the two, but they do coincide, they can be reconciled.

Mr. Lamont: Next I will put in evidence the dividend account. We divided that account into three parts, dividends paid to Mr. Ballagh; dividends paid to Byron Jackson; and dividends paid to Mr. Patterson. That will be Plaintiff's Exhibit 3.

PLAINTIFF'S EXHIBIT No. 3

Plaintiff's Exhibit 1-c

DIVIDENDS PAID TO BYRON JACKSON COMPANY

Year	Check No.	Date	Amount	Total
1928	1747	10/15	$7470.00	$
"	1829	10/25	7470.00	
"	2461	12/17	4980.00	19,920.00
1929	2793	1/18	1245.00	
"	2834	1/26	1245.00	
"	2998	2/25	2490.00	
"	3034	3/2	2490.00	
"	3187	4/2	1245.00	
"	3296	4/15	1245.00	
"	3355	4/30	2490.00	
"	3453	5/10	1245.00	
"	3505	5/23	1245.00	
"	3654	6/11	2490.00	
"	3772	7/8	2490.00	
"	3877	7/17	2490.00	
"	3951	8/1	2490.00	

Dividends Paid to Byron Jackson Company—(Continued)

Year	Check No.	Date	Amount	Total
1929	4068	8/14	$4980.00	$
"	4072	8/14	2490.00	
"	4115	8/22	4980.00	
"	4118	8/31	4980.00	
"	4308	9/20	2490.00	
"	4366	9/30	2490.00	
"	4512	10/21	2490.00	
"	4534	10/25	4980.00	
"	4571	11/1	4980.00	
"	4591	11/6	4980.00	
"	4599	11/8	2490.00	
"	4733	11/20	4980.00	
"	4759	11/26	2490.00	
"	4806	12/4	2490.00	77,190.00
1930	5029	1/3	4980.00	
"	5037	1/4	2490.00	
"	5378	2/25	3735.00	
"	5387	2/28	1245.00	
"	5682	4/10	2490.00	
"	5745	4/23	2490.00	
"	5916	5/27	2490.00	
"	6374	8/15	1245.00	21,165.00
1936	2669	3/16	500.00	
"	3283	8/25	500.00	
"	3391	9/15	500.00	1,500.00
1938	1364	7/7	1500.00	
			Grand Total	$121,275.00

Plaintiff's Exhibit 1-a

DIVIDENDS PAID TO J. C. BALLAGH

Year	Check No.	Date	Amount	Total
1928	1750	10/15	$11,250.00	
"	1842	10/25	11,250.00	
"	2460	12/17	7,500.00	$ 30,000.00
1929	2792	1/18	1,875.00	
"	2833	1/26	1,875.00	

Dividends Paid to J. C. Ballagh—(Continued)

Year	Check No.	Date	Amount	Total
1929	2997	2/25	$3,750.00	
"	3033	3/2	3,750.00	
"	3186	4/2	1,875.00	
"	3294	4/15	1,875.00	
"	3354	4/30	3,750.00	
"	3452	5/10	1,875.00	
"	3504	5/23	1,875.00	
"	3653	6/11	3,750.00	
"	3771	7/8	3,750.00	
"	3875	7/17	3,750.00	
"	3950	8/1	3,750.00	
"	4067	8/14	7,500.00	
"	4070	8/14	3,750.00	
"	4114	8/22	7,500.00	
"	4180	8/31	7,500.00	
"	4306	9/20	3,750.00	
"	4365	9/30	3,750.00	
"	4511	10/21	3,750.00	
"	4532	10/25	7,500.00	
"	4570	11/1	7,500.00	
"	4590	11/6	7,500.00	
"	4597	11/8	3,750.00	
"	4731	11/20	7,500.00	
"	4761	11/26	1,000.00	
"	4762	11/26	2,750.00	
"	4805	12/4	3,750.00	$116,250.00
1930	5028	1/3	7,500.00	
"	5035	1/4	3,750.00	
"	5377	2/25	5,625.00	
"	5385	2/28	1,875.00	
"	5681	4/10	3,750.00	
"	5743	4/23	3,750.00	
"	5914	5/27	3,750.00	
"	6373	8/15	1,875.00	$ 31,875.00
1936	2668	3/16	750.00	
"	3282	8/25	750.00	
"	3426	9/15	750.00	$ 2,250.00
1938	1363	7/7	2,250.00	$ 2,250.00
			Grand Total	$182,625.00

Plaintiff's Exhibit 1-b

DIVIDENDS PAID TO C. L. PATTERSON

Year	Check No.	Date	Amount	Total
1928	1749	10/15	$11,250.00	$
"	1843	10/25	11,250.00	
"	2459	12/17	7,500.00	$ 30,000.00
1929	2791	1/18	1,875.00	
"	2832	1/26	1,875.00	
"	2996	2/25	3,750.00	
"	3032	3/2	3,750.00	
"	3185	4/2	1,875.00	
"	3295	4/15	1,875.00	
"	3353	4/30	3,750.00	
"	3451	5/10	1,875.00	
"	3503	5/23	1,875.00	
"	3652	6/11	3,750.00	
"	3770	7/8	3,750.00	
"	3876	7/17	3,750.00	
"	3949	8/1	3,750.00	
"	4066	8/14	7,500.00	
"	4071	8/14	3,750.00	
"	4113	8/22	7,500.00	
"	4179	8/31	7,500.00	
"	4307	9/20	3,750.00	
"	4364	9/30	3,750.00	
"	4510	10/21	3,750.00	
"	4533	10/25	7,500.00	
"	4569	11/1	7,500.00	
"	4589	11/6	7,500.00	
"	4598	11/8	3,750.00	
"	4732	11/20	7,500.00	
"	4758	11/26	3,750.00	
"	4804	12/4	3,750.00	$116,250.00
1930	5027	1/3	7,500.00	
"	5036	1/4	3,750.00	
"	5376	2/25	5,625.00	
"	5386	2/28	1,875.00	
"	5680	4/10	3,750.00	
"	5744	4/23	3,750.00	
"	5915	5/27	3,750.00	

Dividends Paid to C. L. Patterson—(Continued)

Year	Check No.	Date	Amount	Total
1930	6372	8/15	$1,875.00	$ 31,875.00
1936	2924	3/16	750.00	
"	3281	8/25	750.00	
"	3425	9/15	750.00	$ 2,250.00
1938	1362	7/7	2,250.00	$ 2,250.00
			Grand Total	$182,625.00

DIVIDENDS PAID TO MR. SCHURMAN OR MR. DULIN

Year	Check No.	Date	Amount	Total
1928	1748	10/15	$30.00	
"	1830	10/25	30.00	
"	2462	12/17	20.00	$80.00
1929	2794	1/18	5.00	
"	2835	1/28	5.00	
"	2999	2/25	10.00	
"	3035	3/2	10.00	
"	3188	4/2	5.00	
"	3297	4/15	5.00	
"	3356	4/30	10.00	
"	3454	5/10	5.00	
"	3506	5/23	5.00	
"	3655	6/11	10.00	
"	3773	7/8	10.00	
"	3878	7/18	10.00	
"	3952	8/1	10.00	
"	4069	8/14	20.00	
"	4073	8/14	10.00	
"	4116	8/22	20.00	
"	4182	8/31	20.00	
"	4309	9/20	10.00	
"	4367	9/30	10.00	
"	4513	10/21	10.00	
"	4535	10/26	20.00	
"	4572	11/1	20.00	
"	4592	11/5	20.00	
"	4600	11/11	10.00	

Dividends Paid to Mr. Schurman or Mr. Dulin—(Continued)

Year	Check No.	Date	Amount	Total
1929	4734	11/20	$ 20.00	
"	4760	11/26	10.00	
"	4807	12/4	10.00	310.00
1930	5030	1/3	20.00	
"	5038	1/4	10.00	
"	5379	2/25	15.00	
"	5388	2/28	5.00	
"	5683	4/10	10.00	
"	5746	4/23	10.00	
"	5917	5/27	10.00	$80.00
	Mr. Dulin			
"	6375	8/29	5.00	85.00

[Endorsed]: Filed July 6, 1942.

Mr. Bednar: Just a minute, Mr. Lamont. There is no list of dividends which was paid to——

Mr. Lamont: Mr. Dulin was the president of Byron Jackson.

Mr. Bednar: I am going to object to putting that in. It should be done mathematically.

Mr. Lamont: It is perfectly all right, if you want to make up the total of the capitalization, which is 1,000 shares.

Mr. Bednar: This sheet can be attached.

The Clerk: What are you attaching it to?

Mr. Bednar: To the dividend exhibit which is now in evidence.

The Clerk: Are you offering this?

Mr. Lamont: It may go in as part of mine.

The Clerk: As part of Exhibit 3.

Mr. Lamont: As a matter of fact, I don't think in this [20] phase of the case there is very much doubt about the facts. Then I want to put in evidence Exhibit 13 to the deposition of Mr. Ballagh, which consists of gross and net sales of the company since 1938.

Mr. Bednar: Just a minute.

The Clerk: That will be Plaintiff's Exhibit 4.

PLAINTIFF'S EXHIBIT No. 4

SALES

1938	Jan.	Feb.	Mar.	Apr.	May	June	July	Aug.	Sept.	Oct.	Nov.		Total
Gross	19,045.92	28,020.05	31,864.65	29,876.95	34,812.65	34,919.34	23,665.80	27,201.00	34,136.20	19,529.20	29,907.35		312,979.11
Dis.	2,543.82	3,455.37	3,818.34	4,683.78	4,945.26	5,438.74	2,591.03	3,239.48	4,239.17	2,925.83	3,187.51		41,068.33
Net	16,502.10	24,564.68	28,046.31	25,193.17	29,867.39	29,480.60	21,074.77	23,961.52	29,897.03	16,603.37	26,719.84		271,910.78
1939	Dec. 1938	Jan. 1939	Feb.	Mar.	Apr.	May	June	July	Aug.	Sept.	Oct.	Nov.	Total
Gross	21,832.40	24,561.65	22,944.25	24,265.00	25,151.05	27,956.05	28,303.98	24,427.84	18,935.08	32,410.67	39,576.08	46,163.83	336,527.88
Dis.	2,277.61	4,660.89	4,012.55	1,933.55	3,214.86	3,244.86	2,914.53	4,140.93	1,403.09	3,230.83	4,011.12	5,386.48	40,431.30
Net	19,554.79	19,900.76	18,931.70	22,331.45	21,936.19	24,711.19	25,389.45	20,286.91	17,531.99	29,179.84	35,564.96	40,777.35	296,096.58
1940	Dec. 1939	Jan. 1940	Feb.	Mar.	Apr.	May	June	July	Aug.	Sept.	Oct.	Nov.	Total
Gross	26,385.22	27,309.55	38,658.09	35,267.77	25,259.07	23,705.45	23,415.12	34,044.96	27,923.18	23,428.57	21,418.65	22,805.88	329,621.51
Dis.	3,164.01	2,092.04	4,851.00	2,821.39	2,543.36	1,845.40	1,698.57	2,130.02	1,933.39	1,990.81	1,737.25	1,973.91	28,781.15
Net	23,221.21	25,217.51	33,807.09	32,446.38	22,715.71	21,860.05	21,716.55	31,914.94	25,989.79	21,437.76	19,681.40	20,831.97	300,840.36
1941	Dec. 1940	Jan. 1941	Feb.	Mar.	Apr.	May	June	July	Aug.	Sept.	Oct.	Nov.	Total
Gross	Statement	42,882.04	22,159.93	23,093.52	31,314.71	26,052.36	31,912.18	28,648.53	37,842.21	73,533.09	23,104.74	25,877.56	366,420.87
Dis.	incl. in January	3,675.25	1,697.41	1,686.25	2,717.93	2,460.74	2,730.56	2,617.71	2,575.34	4,343.01	1,491.23	2,338.01	28,333.44
Net		39,206.79	20,462.52	21,407.27	28,596.78	23,591.62	29,181.62	26,030.82	35,266.87	69,190.08	21,613.51	23,539.55	338,087.43

D.C.S.D. Cal. Cent. Div.—Civ. #1762-Y
Byron Jackson Co., Plff. v. Patterson-Ballagh Corp. et al.,
Dfts.
PLAINTIFF'S EXHIBIT 13.

[Seal] MEYER WEISMAN
Notary Public.

[Endorsed]: Filed Jun 29 1942. Edmund L. Smith, Clerk.

[Endorsed]: Filed July 2, 1942.

Mr. Lamont: These have all been supplied by counsel for the defendant. I want to point out one or two things on this. The total sales of 1938, the gross were $312,979.11, and the net was $271,910.78. The gross sales were $336,527, and the net was $296,096.58, in 1939. In 1940 the gross sales were $329,621, and the net sales were $300,840.36. In 1941 the gross sales were $366,420, and the net sales were $338,087.

In other words, since I am introducing that—I don't want to argue my case now, but just to point out to the court that the salaries in 1940 and 1941 were running $50,000 to the two executives on net sales of about $300,000.

Mr. Bednar: Net sales of $300,000 or over.

Mr. Lamont: The net sales were a little bit over in 1941, and probably about an even $300,000 in 1940. There is also one other element, namely, in 1940, in March, the salaries were increased, in March of 1940. Mr. Ballagh's salary was raised $1,000, and in November of that year Mr. Ballagh was given a bonus of one-sixth of his salary, and Mr. [21] Miller was given a bonus of one-sixth of his salary. And in the meantime the gross and net sales of the company were dropping off. In March there were $35,000 of gross sales, and in November $22,000, and a net in March of $32,000 and a net in November of $20,000.

Have you with you the audit, Mr. Bednar, and also the company's statement?

Mr. Bednar: I will see.

Mr. Lamont: I want to put all these three statements in evidence, and I think counsel will probably simplify matters by agreeing with me that the net profits the year 1939 were $20,927.25; in other words, the salaries were twice the net profits.

Mr. Bednar: Counsel, I would rather have the witnesses testify on that. I note here the profits from operations in 1939 were $35,000. If you will tell me what you want——

Mr. Lamont: I don't think there is any need in stipulating. I will put all three in evidence.

Mr. Bednar: That is all right with me, but I want to differentiate between the salaries and the income of the company. I don't want to take a chance of misinterpreting them myself.

Mr. Lamont: They are your own.

Mr. Bednar: That is why I say the first figure you mentioned was the net profit after deduction of certain [22] items, and the other figure I mentioned was a net profit from operation. I would rather have the whole report in.

Mr. Lamont: I am perfectly willing. Mark them one number.

The Clerk: They will be Plaintiff's Exhibits 5-A, 5-B, and 5-C.

Mr. Lamont: We are not disputing the accuracy of what you furnish us at all. I would like to offer these in evidence, which show much larger profits when it came down to the auditing statements. Mark them as Exhibit 6.

The Clerk: These will be Plaintiff's Exhibits 6-A, 6-B, and 6-C.

Mr. Bednar: That was before the computation of taxes and various liabilities.

Mr. Lamont: I desire now to offer in evidence a letter written to Mr. Ballagh, secretary and treasurer of the company, one of the defendants, signed by Mr. Pennington, who was the auditor employed by these two defendants, showing the differential between the company's statement and the audit statement. In other words, according to his letter, there is a difference in 1941 of $12,723; in other words, the company's statements were that much in excess of the auditor's statement. There is also a differential in 1940 of $27,923.28. That is Exhibit 12 to the deposition, which I am offering in evidence now.

Mr. Bednar: Do you want to read that whole letter? [23]

Mr. Lamont: I would like to have the court read it, or shall I read it to the court?

The Court: No. I can read it.

Mr. Lamont: The letter is Exhibit 12 to the deposition, the Ballagh deposition, and the letter is dated January 23, 1942.

Mr. Bednar: Those exhibits are not included in this deposition.

Mr. Lamont: Here they are.

The Clerk: That will be Plaintiff's Exhibit 7.

PLAINTIFF'S EXHIBIT No. 7

D.C.S.D. Cal. Cent. Div. Civ. #1762-Y. Byron-Jackson Co., Plff. vs. Patterson-Ballagh, Corp., et al., Dfts. Plaintiff's Exhibit No. 12. (two sheet).

[Seal] MEYER WEISMAN
Notary Public

Telephone Jefferson 3145 Teletype L. A. 591

[Cut: Moulded Rubber and Plastics—Oil Field Specialties]

PATTERSON - BALLAGH
Corporation
1900 East Sixty-Fifth Street
Los Angeles, Calif.
January 23, 1942

Mr. J. C. Ballagh, Secretary-Treasurer
Patterson-Ballagh Corporation
1900 East 65th Street
Los Angeles, California

Dear Mr. Ballagh:

With reference to our recent conversation with Mr. Burrell, regarding the differences between the surplus net earnings as shown on the preliminary report for fiscal years ended November 30, 1941 and 1940, the writer desires to make the following explanation.

Fiscal year ended 11/30/41

The surplus net earnings as shown for November 30th, prior to special audit, showed $35,722.73, and the audit report showed surplus net gain of $22,998.94, a difference of $12,723.79.

These differences are accounted for, shown as follows:

Cost of Sales	2,450.88*
Obsolescence	3,426.12
Depreciation—Warehouse Furnishings and Fixtures	243.86
Bad Debts Written Off	76.60
Royalties—Adjustment	260.12*
Royalties—Contingent	8,887.50
Machinery Depreciation—Adjustment	1,343.47
Installation Tools—Depreciation Adjust.	1,701.10
Total	$12,723.79

* Figures in red.

Fiscal year ended 11/30/40

The chief differences for fiscal year ended 11/30/40 of $27,-723.78 consisted chiefly of inventories adjustments of $27,854.89. In explaining these differences, desire to state that in changing over the system of accounting at the time that the writer came into the picture as auditor for the corporation, and in order to have as near as possible a correct inventory, it was necessary to decrease the inventory by an amount of $9,628.32. This was a decrease from the amount as shown on the November 30, 1940 preliminary financial statement for fiscal year ended 11/30/40.

There was an adjustment of Receivables,—one item of consigned merchandise (Turner Valley Supply Company, Canada) of $4,397.90; Bad Debts Written Off, $1,136/74; Depreciation Adjustments of $3,917.04 and Contingent Liability of $8,782.50. The balance of the amount of the total differences consisted of minor adjustments made in the various accounts to bring them down to actual.

Trusting this fully explains the differences after special audit for 1940, I am

Very truly yours,
JOSEPH "H" PENNINGTON
Joseph "H" Pennington
Certified Public Accountant

[Endorsed]: Filed June 29, 1943.

[Endorsed]: Filed July 2, 1942, by Cross, dep. clerk.

Mr. Lamont: I now place in evidence another letter written by Mr. Dulin to Patterson-Ballagh at a different time. I next offer in evidence—this is Exhibit 7 to the deposition we have just been referring to—a letter written by Mr Dulin to Mr. Ballagh, dated February 1, 1937.

Mr. Bednar: Just a minute.

Mr. Lamont: This is Exhibit 7 referred to in the deposition.

Mr. Bednar: That is not the original.

Mr. Lamont: I think I demanded the original from you. Is there any question about that being a copy?

Mr. Bednar: Here is the original.

Mr. Lamont: We will put the original in, then.

The Clerk: That will be Plaintiff's Exhibit 8.

Mr. Lamont: It reads:

"February 1, 1937 [24]

"Mr. J. C. Ballagh, Secretary
"Patterson-Ballagh Corporation
"1900 East 65th Street
"Los Angeles, Calif.

"Dear Jack:

"Referring to the recent stockholders' meeting, in connection with the resolution approving the acts of record of the officers and directors during the past year, I wish to state that I am agreeable to the approval of such resolution, provided there is inserted in the minutes that I do not approve those acts which I have previously disapproved or objected to.

"From the preliminary financial statement rendered, I also wish to state that in my opinion the company's financial condition has not allowed the administrative salaries being paid which in my opinion are excessive and further, the dividends declared during the year should not have been paid.

Taking into consideration the condition of the business, the volume of sales, as a director and a stockholder, I urge that the administrative salaries be adjusted downward and that no further dividends be paid until the company is in a greatly improved financial condition."

Mr. Bednar: That letter was written about a year prior to the period in controversy. [25]

Mr. Lamont: I next want to offer in evidence a letter dated March 23, 1937, addressed by Mr. Dulin to Mr. Patterson. The letter is dated March 23, 1937. I will offer it in evidence.

The Clerk: That will be Plaintiff's Exhibit 9.

Mr. Lamont:

"Mr. C. L. Patterson, President
"Patterson-Ballagh Corporation, Ltd.
"1900 E. 65th St.
"Los Angeles, Calif.
"Copy to Mr. J. C. Ballagh, Secretary.

"My Dear Pat:

"I have just heard that you are contemplating shutting down the factory in the near future. The reason for doing so, I am not conversant with. It is probably due to one or a combination of the following: finances, current business, or labor difficulties. In the past, I have requested current financial statement promptly and for some reason they have not been forthcoming.

"In the past, I have stated very definitely my views as to executive salaries, dividends, etc. These have been disregarded and I have been in the minority; therefore, the operators of the company being a majority of the directors and recipients of (in my opinion) unwarranted high [26] salaries. In the procedure that you follow, the responsibility for same is clearly up to the majority of stockholders and the directors who have voted in favor of the acts that I have complained of. Representing a substantial percentage of the stock and as a director, I resent these acts and do not in any way release the majority directors from the libility entailed.

"I do not know whether you are temporarily closing the plant or if it is to be a permanent nature and liquidation of the business. Therefore, if any such act is planned at this time, you should call a directors meeting at a time that is mutually convenient so that these matters of importance may be presented to the board. If the majority operating directors are going to continue to operate the business at they see fit without even calling directors meetings on vital points, I, in behalf of the stock which I represent will hold those majority directors accountable."

Mr. Bednar: That is a letter of March, 1937?

Mr. Lamont: Yes.

Mr. Bednar: That is the year Mr. Dulin voted for a dividend and voted for $1500 a month.

Mr. Lamont: Take a look at the profits during that [27] period.

The next is a night letter, marked Plaintiff's Exhibit 5 to the deposition, and I am offering that in evidence. It is dated September 25, 1938.

The Clerk: That will be Plaintiff's Exhibit 10.

Mr. Lamont: It reads as follows:

"Patterson Ballagh Corp.
"1900 East 65 St.
"Losa

"Notice directors meeting twenty-seventh just received. Object to action this meeting Paragraph number three reference increasing officers salaries as desire to be present when discussed and voted upon stop Recent policy of company to have regular monthly meeting certain specified time I was available then and now special meeting called in my absence."

It is signed "E. S. Dulin."

The next letter I offer is one dated July 20, 1939, which is marked Plaintiff's Exhibit 4 to the deposition. I offer it in evidence.

The Court: All right.

Mr. Lamont: It reads as follows.

The Clerk: Let me have it to mark, please.

Mr. Bednar: What is the number?

Mr. Lamont: It is Exhibit 4 to the deposition.

The Clerk: That will be Plaintiff's Exhibit No. 11. [28]

Mr. Lamont: It reads as follows:

"Since my letter to you of June 27, I have been away from the office a great deal on a vacation period. However, during this interim, I have had an opportunity of going over the corporation's statement for May, 1939, and note that executive salaries for the month of May were $3,000. Upon comparison with April, I find the same item at $2,000. Today I have reviewed the minutes of the directors meeting of February 15, 1939, particularly that resolution on page 8 thereof. At the directors meeting held June 27, there was no discussion or even mention of any change in the officers' salaries.

"Awaiting your explanation on the foregoing, I am,

"Yours very truly."

I am next offering a letter dated September 8, 1939. I offer as Exhibit 12 a letter of September 8, 1939. That was Exhibit 3 to the deposition.

The Clerk: That will be Plaintiff's Exhibit No. 12.

Mr. Lamont: It reads as follows. It is addressed to the Patterson-Ballagh Corporation:

"Attention of Mr. J. C. Ballagh [29]

"Gentlemen:

"On your balance sheet for July 31, 1939, under Current Assets, I would appreciate it if you would advise me what the following item consists of:

'Fund Account, $1,711.78.'

"I have just noted the copy of the minutes of your meeting of August 22 which accompanied your letter of September 6. This is the meeting that I was unable to attend. I note that the compensation of the secretary and treasurer was increased $4,000 per year. Taking into consideration the present condition of the company, the earnings so far attained this year, the prospects for the future, and further, Mr. Miller's remarks at a previous meeting in connection with profits, I feel very definitely that the executive salaries of the Patterson-Ballagh Corporation should not be increased. I regret that it was impossible for me to be at the meeting so that I could object to this increase, which I do not believe, from all information I have at hand, is warranted at this time."

The next letter I offer is a letter dated February 25, 1941.

Mr. Bednar: Which one is that?

Mr. Lamont: It is Exhibit 9 to the deposition. It [30] will be Exhibit No. 13, will it not?

The Clerk: Plaintiff's Exhibit 13.

Mr. Lamont: It reads as follows: It is addressed to Mr. Miller.

"Dear Mr. Miller:

"I have just returned from the East and note your letter of the 19th enclosing the public accountants' statement for Patterson-Ballagh Corporation for the year ending November 30, 1940. I have not had a chance to study same, but at a quick glance, note that the profit figures as ren-

dered by the above referred to accountants are at great variance with the company figures which you had available at the time of your November meeting and its adjournment, at which time you voted Mr. Ballagh and yourself and other employees substantial bonuses. The company's statement before taxes on income as of November 30, 1930"—it reads "1930"; I think it means "1940"—"which was rendered to the directors shows a profit of approximately $51,000, compared to the public accountants' figures of approximately $23,000.

"As soon as I have time, I will give further study to the report. In the meantime, if you could advise me as to the large discrepancy be- [31] tween the company's figures and the public accountants', it would be welcome.

"Yours very truly."

I then offer in evidence a letter dated June 25, 1941, addressed to the Patterson-Ballagh Corporation, and marked Exhibit 2 to the deposition. I thing the original was attached, because I have a photostat of the original. That letter went in twice in the deposition. It went in as a copy and also the original. I am offering it.

The Clerk: It will be Plaintiff's Exhibit 14.

Mr. Lamont:

"Patterson-Ballagh Corporation

"1900 E. 65th St.

"Los Angeles, Calif.

"Attention: J. C. Ballagh, Secretary.

"Gentlemen:

"I beg to acknowledge your letter of the 19th enclosing the May statement, from which I note that you were just able to keep your head above water as far as earnings are concerned when taking into consideration the excessive administrative salaries, which are certainly not justified by the showing made.

"On February 25, 1941, I wrote Mr. Miller, asking for some enlightenment as to the great discrepancy between company earnings and the figures by the auditors for last year. If you will recall, [32] it was the company's figures upon which you based salary increases, bonuses, and other expenditures. It would seem to me that you have had plenty of time to advise me in this connection and I would appreciate a reply.

"One of the conditions and justifications for your acts was that these salaries would be promptly adjusted downward should the trend of earnings (as represented) change from what was prevailing at that time. Your audit results show that you did not have the earnings as represented and certainly the company's figures for this year do not show any justification for same."

I wish now to place in evidence—I have copies here, and I am going to ask counsel to stipulate,

subject to the right of correction, that the four exhibits in the complaint in civil action pending in this court, numbered 1087-H, which are the four agreements making up the license patent arrangement that existed between Byron Jackson and Patterson-Ballagh——

Mr. Bednar: You are asking now concerning these four documents?

Mr. Lamont: I am offering them in evidence. It is all a matter of record in this court.

Mr. Bednar: The question that occurs to my mind is this: That was a long, complicated case, and we can put in [33] only part——

Mr. Lamont: We are perfectly willing to put the entire record in, if you want it. We would be delighted to.

Mr. Bednar: It seems to me it encumbers the record to put all this other in. So far as these original agreements are concerned, if we have a right to check the agreements, I have no objection to them going in, but how much further we should go I frankly don't know.

Mr. Lamont: All I intended to offer were these four agreements, along with your repudiation of June 30, 1939. That was an exhibit to your answer. I was going to stop there. If you want anything else in from that record, we would be delighted to have it.

Mr. Bednar: Those four agreements, plus that repudiation. The trial lasted a long time, and there were over a hundred pages of briefs.

The Court: This is only for a limited purpose?

Mr. Lamont: Simply to show that, as part of the same idea, Mr. Miller came in and repudiated our license agreement and stopped paying dividends and raised salaries.

Mr. Bednar: Where is the stock book?

Mr. Lamont: I thought it was there. I thought I had copies of it. I think it is Exhibit 5, is it?

Mr. Bednar: No.

Mr. Lamont: I have copies here. Here is a copy. I don't care anything about 6, unless you want it. [34]

Mr. Bednar: No. Subject to correction, and with the stipulation that the pencil notations appearing on these will be disregarded——

Mr. Lamont: You can disregard those. And also I have marked them exhibit so-and-so, applying to the other case.

The Clerk: They will be Plaintiff's Exhibits 15-A, 15-B, 15-C, and 15-D.

PLAINTIFF'S EXHIBIT No. 15-A

[Written in pencil, top margin]: Exclusive License to Pat.-Bal. under Hopkins patent. 8 copies.

(Copy of Original Agreement)

AGREEMENT

This Agreement, made and entered into this 20th day of September, 1928, by and between Byron Jackson Pump Company, a corporation of Delaware, having a place of business at Los Angeles, California, hereinafter called the Licensor, and Patterson-Ballagh Corporation, a corporation of Califor-

nia, having its place of business at Los Angeles, California, hereinafter called the Licensee,

Witnesseth:

That Whereas, Licensor is the owner of U. S. Letters Patent No. 1,619,728, issued March 1, 1927 to Arthur C. Hopkins for cushion joint for rotary drill pipes;

[Printer's Note: Hopkins written in pencil above figures 1,619,728.]

And Whereas, Licensee is desirous of acquiring the exclusive right, liberty, license and privilege to make, use and sell the inventions, devices and things claimed and patented in and by said Letters Patent No. 1,619,728, together with any improvements thereon made and acquired by the Licensor and any letters patent which may issue therefor, or any reissue, division or extension thereof;

[Printer's Note: Hopkins written in pencil opposite figures 1,619,728.]

Now, Therefore, in consideration of the sum of one dollar ($1.00) paid by the Licensee to the Licensor, receipt whereof is hereby acknowledged, and of the mutual covenants contained herein, and for other good and valuable considerations, the parties hereto have agreed as follows:

1. The Licensor grants and conveys to the Licensee, its successors, legal representatives and assigns, subject to the terms and conditions and covenants hereinafter set forth, the exclusive right, liberty, privilege and license to manufacture, use and sell to others to use throughout the United States and all the territories thereof, and all foreign countries,

the invention or inventions, devices and things disclosed, claimed and patented in said Letters Patent No. 1,619,728, granted March 1, 1927 to said Arthur C. Hopkins for cushion joint for drill pipes, and throughout the whole term for which said Letters Patent have been issued, together with any re-issue, division or extension thereof, with any improvements thereon made or acquired by Licensor.

[Printer's Note: Hopkins written in pencil above figures 1,619,728.]

2. The Licensee agrees to pay to the Licensor a royalty or license fee of twenty-five cents (25c) on each and every well casing protector sold by the Licensee and which contains or embodies the invention or inventions of any claim or claims of said Letters Patent No. 1,619,728, or of Letters Patent No. 1,573,031, issued February 16, 1926, to one William I. Bettis, on application of said Bettis and one Leroy H. Perry, and which device, thing or invention shall be so sold to be used on well drill pipe or the joints or couplings thereof; and, similarly, to pay a royalty or license fee equal and equivalent to fifteen percent (15%) of the net proceeds of sale of all such devices of both said Letters Patent Nos. 1,619,728 and 1,573,031, sold by the Licensee for any other kind or purpose of use, of which said fifteen percent (15%) of net proceeds one-half shall be paid to Licensor and one-half to said William I. Bettis, owner of said Bettis patent, in amplification of royalties or license fees heretofore agreed to be paid to him by Licensee; ~~and also Licensee agrees to pay to Licensor for all tool joints and drill collars, minus~~

~~cushions, sold by Licensee and containing or em-~~ bodying any invention, device or thing claimed and patented in and by said Letters Patent No. 1,619,728, namely, twenty-five cents (25c) for each such last mentioned device or thing three inches (3″) or under in standard diameter, fifty cents (50c) for each such last mentioned device or thing over three inches (3″) and under five inches (5″) in standard diameter, and seventy-five cents (75c) for each such latter device or thing five inches (5″) and over of ~~standard diameter~~.

[Printer's Note: Hopkins written in pencil above figures 1,619,728. Bettis written in pencil above figures 1,573,031. Initials C.L.P., R.S., J.C.B. typed in left-hand margin.]

3. Each such royalty or license fee as specified and named in the paragraph numbered "2" hereof shall be paid by the Licensee to the Licensor on the 25th day of each and every calendar month from and after November 1, 1928, and computed and calculated upon the devices, things and inventions sold and delivered by the Licensee within the scope and meaning of this license, during the preceding calendar month; and such payments and each thereof shall be made to Licensor at its place of business at Los Angeles, California.

4. The Licensee covenants and agrees to deliver to the Licensor at its said Los Angeles address, on or before the 25th day of each calendar month during the life of this agreement, a true statement in writing setting forth the number of licensed devices, inventions or things manufactured and sold

by or on behalf of licensee during the preceding calendar month, together with the names of the purchasers thereof. The Licensee also agrees that it will, upon demand of the Licensor, cause any such statement made by the Licensee to be verified under oath by an officer of the Licensee, or the Licensor by its agent may at any time during business hours have access to the books of Licensee to check and audit same.

5. Should the Licensee be sued by any third party for the infringement of any patent because of the manufacture by the Licensee of any device, thing or invention claimed and patented in and by said Letters Patent No. 1,619,728, the Licensee agrees to defend said suit at the joint cost and expense of Licensor and Licensee.

6. Should the Licensee desire to bring suit against any infringer of said patent No. 1,619,728, the Licensor agrees that said suit may be brought in its name or in the name of the then owner or owners of all right, title and interest in and to and under said Letters Patent No. 1,619,728, or both in such name or names and the name of Licensor, either with or without the name of Licensee, and it agrees to assist in all reasonable ways in the preparation and prosecution of said suit, at the joint cost and expense of the Licensor and Licensee, and that in such event the Licensor and Licensee shall receive any damages or profits or both awarded in such suit share and share alike.

7. It is agreed that in the event the Licensee should be adjudged a bankrupt, then and in such

an event the Licensor may terminate this agreement if it so desires, and all rights granted herein and hereby shall be relinquished and surrendered by the Licensee and revert back to the Licensor.

8. Time is the essence of this agreement, and should either party hereto fail to make good any default hereunder, within thirty days of receipt from the other party of written notice of default, it is agreed that this agreement may thereupon be terminated against the defaulting party by the mailing

its

to said defaulting party at is last known address, by the other party, Licensee or Licensor, as the case may be, of a written notice so terminating this agreement.

9. The Licensee agrees to advertise said well casing protectors from time to time in leading oil trade journals, to that end employing the names "Bettis" and "Hopkins" in identification of such well casing protectors, and will use aggressive sales methods aimed at bringing the said well casing protectors before the different oil operators and producers, and will use its best efforts to create a demand for said devices.

10. The Licensee agrees to conspicuously mark each and every thing, device or invention made or caused to be made and sold by it under the license or any license or privilege of this agreement, with the number and date of said Hopkins patent, to wit, No. 1,619,728, March 1, 1927, and the number and date of said Bettis patent, to wit, No. 1,573,031, February 16, 1926.

11. The Licensee shall supply all reasonable demands of the public for said well casing protectors as licensed herein and hereby, and should the Licensee fail to supply such demand, this agreement may be terminated at the option of the Licensor upon service of a sixty days' notice in writing upon the Licensee.

This agreement made in triplicate.

Signed at Los Angeles, County of Los Angeles, State of California, this 20th day of September, 1928, said corporations hereunto affixed their corporate signatures by their respective presidents and their corporate seals attested by their respective secretaries, each duly authorized by their respective boards of directors.

BYRON JACKSON PUMP
COMPANY
By ROBERT SCHURMAN (Signed)
Vice Pres.

Seal:
Attest:
H. J. ELLEN (Signed)
Secretary

PATTERSON-BALLAGH
CORPORATION
By C. L. PATTERSON (Signed)
President

Seal:
Attest:
J. C. BALLAGH (Signed)
Secretary

Endorsement by William I. Bettis

In consideration of the payments agreed to be made, and to be made to me pursuant to the terms of the foregoing agreement, I do hereby endorse and approve same under and pursuant to agreement between myself and said Licensee made and entered into December 2d, 1927, said Licensee being therein stated as comprising C. L. Patterson and J. C. Ballagh, and payments to me under which latter agreement and as therein expressed and provided shall continue. It is expressly understood that this endorsement shall in no way affect reduce the royalties agreed upon between myself and said C. L. Patterson and J. C. Ballagh, under the License Agreement entered into December 2nd, 1927.

[Printer's Note: W.I.B. typed in right-hand margin, and circled in pencil; also the word "affect" circled in pencil and marked out in purple ink.]

Dated: September 20th, 1928.

(Signed) W. I. BETTIS

[Endorsed]: Filed July 2, 1942.

PLAINTIFF'S EXHIBIT No. 15-B

[Written in pencil, top margin]: Exclusive License to BJCO to sell all metal Hopkins Joints under Bettis Patents. 8 copies.

(Copy of Original Agreement)

AGREEMENT

This Agreement made and entered into this 20th day of September, 1928, by and between Patterson-Ballagh Corporation, a California corporation, with its principal place of business at Los Angeles, California, herein called the party of the first part, and Byron Jackson Pump Co., a Delaware corporation, with its principal place of business at West Berkeley, California, herein called the party of the second part.

Witnesseth

Whereas, the party of the first part is the sole Licensee for the manufacture and sale of the Bettis Casing Protector under United States Letters Patent No. 1,573,031, hereinafter called "Bettis Patent", and

Whereas, the party of the second part is the owner of United States Letters Patent No. 1,619,728, described as the Hopkins Patent for Cushion Joint, and hereinafter called "Hopkins Patent", and

[Printer's Note: Written in pencil, left-hand margin]: ½ interest in this patent assigned to Patterson-Ballagh Dec. 29, 1931 whereby they receive ½ of the royalties.

Whereas, the second party has granted unto the said first party an exclusive license of even date

herewith, granting to said second party the sole right to manufacture, use and sell devices under United States Letters Patent No. 1,619,728, described as the Hopkins Patent for Cushion Joint, and

Whereas, the second party is desirous of obtaining the exclusive right, liberty and license to make, use and sell the inventions, devices and things claimed and patented under and by said Letters Patent No. 1,619,728, together with any improvements thereon made and acquired by said first party and any Letters Patent which may issued therefor or any reissue, division or extension thereof,

Now Therefore, in consideration of the premises and performance of the covenants and agreements herein exchanged, it is agreed between the parties hereto, as follows:

1. The first party grants and conveys to the Licensee, its successors, legal representatives, assigns and sublicensees, subject to the terms and conditions and covenants hereinafter set forth, the exclusive right, liberty privilege and license to manufacture, use and sell to others to use, throughout the United States and all the territories thereof, and all foreign countries, the part or parts of the invention or inventions, devices and things disclosed, claimed and patented in said Letters Patent No. 1,619,728, that is or are made of steel or other metal, for the full term of said Letters Patent, together with any reissue, division or extension thereof with any improvements thereon made or acquired by Licensor, the said party of the first part reserving

to itself, its successors in interest and assigns the right to manufacture and furnish all rubbers or cushions of every kind and nature, excepting steel or other metal, used in connection with the manufacture of said devices under said Hopkins Patent. And the said party of the second part agrees for itself, its successors in interest, assigns and sublicensees, that it and they will purchase all rubbers or cushions of every kind and nature, excepting steel or other metal, used in connection with the manufacture, sale and use of Hopkins Joints from said first party.

2. It is hereby understood and agreed by and between the parties that this is a paid-up license and that the consideration for the granting of this license is that the second party, its successors in interest and assigns and sublicensees, are hereby obligated to purchase all cushions to be used in connection with the devices manufactured and sold hereunder from said first party.

3. The said second party agrees to keep true and accurate books of account showing the number of said devices manufactured and sold hereunder, which books of account shall be open during all usual business hours for the inspection of the first party or his authorized agent; the said second party agrees to render monthly a statement in writing to the first party on the twenty-fifth day of each and every month during the term of this license, setting forth a true statement of the number of Hopkins Cushion Joints sold by it and its sublicensees during the preceding month.

4. The licensee agrees that each of said Hopkins Cushion Joints manufactured and sold hereunder shall be marked with the word "Patented" together with the number of said Hopkins Patent, to-wit, No. 1,619,728.

In Witness Whereof the parties hereto have caused this agreement to be executed in their respective names by duly authorized officers, and their respective corporation seals to be hereto attached.

PATTERSON BALLAGH
CORPORATION
By C. L. PATTERSON (Signed)
President

Seal:
Attest:
J. C. BALLAGH (Signed)
Secretary

BYRON JACKSON PUMP CO.
By ROBT. SCHURMAN (Signed)
Vice President

Seal:
Attest:
H. J. ELLEN (Signed)
Secretary

[Endorsed]: Filed July 2, 1942.

PLAINTIFF'S EXHIBIT No. 15-C

Agreement to sell ½ Hopkins pat. to Patterson & Ballagh

(Copy of Original Agreement)

AGREEMENT

This Agreement made and entered into this 20th day of September, 1928, by and between Byron-Jackson Pump Co., a Delaware corporation with offices at the City and County of San Francisco, State of California, Party of the First Part, and C. L. Patterson and J. C. Ballagh, both of the City of Los Angeles, County of Los Angeles, State of California, Parties of the Second Part,

Witnesseth:

Whereas, the said party of the first part is the sole and exclusive owner of United State Letters Patent No. 1,619,728 issued March 1, 1927, to Arthur C. Hopkins for Cushion Joint for Rotary Drill Pipe, and

Whereas, the said party of the first part did, on the 20th day of September, 1928, grant unto Patterson-Ballagh Corporation, a California corporation, having its principal place of business at Los Angeles, California, the exclusive right, liberty, license and privilege to make, use and sell the inventions, devices and things claimed and patented in and by said Letters Patent, and

Whereas, the said party of the first part is also the owner of certain new and useful inventions in drill pipe couplings and applications for United

States Letters Patent Serial No. 77,272 filed December 23, 1925, and Serial No. 111,491 filed May 25, 1926, for the same, and known as the Hardesty applications, and

Whereas, the said parties of the second part are desirous of purchasing an undivided one-half interest in and to United States Letters Patent No. 1,619,728 and an undivided one-half interest in and to that certain License Agreement between the said party of the first part, licensor, and the Patterson-Ballagh Corporation, licensee, and dated September 20, 1928, and mentioned above:

Now, Therefore, in consideration of the premises and the covenants and agreements hereinafter contained by both parties to be kept and performed, the parties do hereby agree together as follows:

I.

The said party of the first part hereby agrees to sell to the said parties of the second part an undivided one-half interest in and to United States Letters Patent No. 1,619,728 issued March 1, 1927, and an undivided one-half interest in and to that certain License Agreement of date September 20, 1928, by and between the party of the first part, Licensor, and Patterson-Ballagh Corporation, Licensee, for the sum of Thirty-seven Thousand Five Hundred ($37,500.00) Dollars and other good and valuable considerations this day passing from said parties of the second part to said party of the first part, the said sum of Thirty-seven thousand Five Hundred ($37,500.00) Dollars to be paid as follows, to wit:

The said party of the first part shall collect all royalties due and payable from the said Patterson-Ballagh Corporation under the term and condition of said License Agreement between the party of the first part, Licensor, and said Patterson-Ballagh Corporation, parties of the second part, Licensee, until said party of the first part has received the total sum of Seventy-Five Thousand ($75,000.00) Dollars. When said party of the first part has received from said royalties under said License Agreement the sum of Seventy-five Thousand ($75,-000.00) Dollars, then it agrees to convey to said parties of the second part by good and sufficient assignments an undivided one-half interest in and to said United States Letters Patent No. 1,619,728 and an undivided one-half interest in and to said License Agreement, and after that date the said party of the first part shall receive one-half of all royalties under said contract and the said parties of the second part shall receive the other half of said royalties, share and share alike.

II.

It is further understood and agreed by and between the parties hereto that in the event of patent infringement litigation by the Patterson-Ballagh Corporation on either the Hopkins Patent No. 1,-619,728 or the Bettis Patent No. 1,573,031, that if any advantage could be obtained by said Patterson-Ballagh corporation under any patent, or patents, that may issued under the Hardesty applications, Serial No. 77,272 filed December 23, 1925, and Serial No. 111,491 filed May 25, 1926, then, and in that

event, the said party of the first part will extend to the said Patterson-Ballagh Corporation all such benefits and advantages under any and all patents which may issued to them under said applications for Letters Patent.

III.

It is understood and agreed by and between the parties hereto that each of the parties hereby give to the other the right and privilege to inspect their respective books and accounts pertaining to all business having to do will all devices manufactured or sold under this agreement.

In Witness Whereof the party of the first part, by its duly authorized officers has caused these presents to be executed and the said parties of the second part have hereunto set their hand this 20th day of September, 1928.

BYRON JACKSON PUMP CO.

(Signed) By ROBERT S. SCHURMAN
Vice Pres.

(Signed) By H. J. ELLEN [Seal]
Secretary

(Signed) C. L. PATTERSON

(Signed) J. C. BALLAGH

[Endorsed]: Filed, July 2, 1942.

PLAINTIFF'S EXHIBIT No. 15-D

Stock Purchase & Option

(Copy of Original Agreement)

This Agreement, made and entered into this 20th

day of September, 1928, by and between C. L. Patterson and J. C. Ballagh, both of Los Angeles, hereinafter called First Parties, and Byron Jackson Pump Co., a Delaware corporation, with its principal place of business in San Francisco, California, hereinafter called Second Party,

Witnesseth:

Whereas, First Parties are the owners of all of the shares (excepting one share) of the capital stock of Patterson-Ballagh Corporation, a California corporation, with its principal place of business in Los Angeles, California, and

Whereas, Second Party has entered into a contract with said Patterson-Ballagh Corporation for the manufacture and sale of a certain cushion joint (U. S. Letters Patent #1,619,728), and desires to purchase from First Parties part of their stock holdings in said Patterson-Ballagh Corporation,

Now, Therefore, in consideration of the premises and of the covenants and agreements of the parties hereto as hereinafter set forth, said parties do hereby convenant and agree as follows, to wit:

1. First Parties agree to sell to Second Party and Second Party agrees to purchase of First Parties Two Hundred and Fifty (250) shares of the capital stock of the said Patterson-Ballagh Corporation for the sum of Twenty-five Thousand Dollars ($25,000.00) and to pay said sum to First Parties at Los Angeles, California, on or before September 20, 1928, upon the delivery of a certificate or certificates in the name of Second Party and

representing said Two Hundred and Fifty (250) shares, First Parties representing and agreeing that said Two Hundred and Fifty (250) shares shall constitute a one-fourth (¼) interest in said corporation. In the event that said sum of Twenty-five Thousand Dollars ($25,000.00) is paid by Second Party to First Parties on or before September 20, 1928, as contemplated by the terms of this paragraph, Second Party shall be entitled to receive all dividends declared at any time on or after September 1, 1928, upon said Two Hundred and Fifty (250) shares.

2. First Parties hereby give and grant to Second Party an option to purchase of and from First Parties additional shares of the capital stock of said Patterson-Ballagh Corporation, such additional shares to be not less than One Hundred and Twenty-five (125) shares and not to exceed Two Hundred and Fifty (250) shares, (as may be determined by Second Party subject to paragraph 4 of this agreement) at the price of One Thousand Dollars ($1,000.00 per share, payable upon the delivery to Second Party by First Parties of a certificate or certificates standing in the name of Second Party and representing the number of shares as to which said option has been exercised, said option to be exercised and only to be exercised upon September 1, 1929, or upon September 15, 1929, or upon any date between said two last mentioned dates, by written notice by Second Party to First Parties either served upon First Parties personally or left, addressed to First Parties, at the office of said Patterson-Ballagh Corporation in the City of Los An-

geles, or mailed, postage prepaid, to First Parties at their last known addresses. First Parties agree that Second Party shall be given the opportunity at any time subsequent to September 1, 1929, and prior to September 15, 1929, to audit the books of said Patterson-Ballagh Corporation. First Parties represent and agree that, in the event of the exercise of said option, Two Hundred and Fifty (250) shares will, at the time of the transfer to Second Party of additional shares in accordance with the terms of said option, constitute a one-fourth (¼) interest in said corporation.

3. In the event that Second Party shall exercise said option granted to Second Party by paragraph 2 of this agreement and in the further event that the net profits of said Patterson-Ballagh Corporation for the twelve (12) months' period from September 1, 1928, to September 1, 1929, (computed in the manner that net profits have been ordinarily computed by said Patterson-Ballagh Corporation but before deduction for Federal income taxes) shall exceed the sum of Two Hundred Tousand Dollars ($200,000.00) then the purchase price for the number of shares so to be purchased under said option shall, in lieu of One Thousand Dollars ($1,000.00) per share, equal the number of shares so to be purchased multiplied by One Thousand Dollars ($1,000.00) less a fractional amount of such excess the numerator of which faction shall be the number of shares to be purchased and the denominator of which shall be One Thousand (1,000).

4. The option given Second Party by paragraph 2 of this agreement, irrespective of anything here-

tofore contained to the contrary, shall not bestow upon Second Party a right to purchase a number of shares of the capital stock of said Patterson-Ballagh Corporation which if added to the Two Hundred and Fifty (250) shares to be purchased under paragraph 1 of this agreement would give Second Party a greater interest in said corporation than the proportion that the net sales by said Patterson-Ballagh Corporation under the "Hopkins" Patent (to wit, U. S. Patent #1,619,728) plus one-half (½) of the net sales to the customer by either Patterson-Ballagh Corporation or by Second Party of any devices the manufacture of which shall hereafter commence under either the "Bettis" Patent (to-wit) U. S. Patent # 1,573,031) or the said "Hopkins" Patent, plus one-half (½) of said net sales to the customer by either Patterson-Ballagh Corporation or by Second Party of any devices the manufacture of which shall hereafter commence under either the said "Bettis" Patent or the said "Hopkins" Patent plus the net sales of said Patterson-Ballagh Corporation under the said "Bettis" patent. The term "net sales" as used in this paragraph shall mean net sales for the months of June, July and August, 1929.

5. In addition to the option given Second Party by the provisions of paragraph 2 hereof, and in the event that on or before September 20, 1928, Second Party pays to First Party the sum of Twenty-five Thousand Dollars ($25,000.00), (said last mentioned sum of Twenty-five Thousand Dollars ($25,000.00) being in addition to the sum of Twenty-five Thou-

sand Dollars ($25,000.00) mentioned in paragraph 1 hereof), First Parties do hereby give and grant to Second Party the option to purchase of and from First Parties Two Hundred and Fifty (250) shares of the capital stock of said Patterson-Ballagh Corporation at the price of One Thousand Dollars ($1,000.00) per share, said sum of Twenty-Five Thousand Dollars ($25,000.00) to apply on said purchase price in the event of the exercise of said option, provided, however, that the option given by this paragraph shall be exercised and shall only be exercised on or before March 20, 1929, by written notice by Second Party to First Parties either served upon First Parties personally or left, addressed to First Parties, at the office of said Patterson-Ballagh corporation in the City of Los Angeles, or mailed, postage prepaid, to First Parties at their last known addresses. The purchase price of said shares as in this paragraph provided shall be paid by Second Party to First Parties upon the delivery by First Parties to Second Party of a certificate or certificates standing in the name of the Second Party and representing said Two Hundred and Fifty (250) shares, (First Parties to have until the 5th day of January, 1929, to deliver said certificate or certificates and no right to receive any dividend or dividends upon said last mentioned shares shall accrue to Second Party until the actual delivery of said certificate or certificates), Second Party agreeing upon the delivery of said certificate or certificates to immediately assign or cause to be assigned to said Patterson-Ballagh Corporation said "Hop-

kins'' Patent, together with those certain applications for Letters Patent (or Patents, if theretofore issued thereunder) numbered and filed as follows, to wit: Serial #77272, filed December 23, 1925, for Drill Pipe Couplings, Serial #111491, filed May 25, 1926, for Drill Pipe Couplings, and Serial #118114, filed May 2, 1927, for Drill Pipe Couplings. First Parties furthermore represent and agree that, in the event of the transfer to Second Party of said Two Hundred and Fifty (250) shares in accordance with the provisions of the option given by this paragraph, said Two Hundred and Fifty (250) shares shall constitute a one-fourth (¼) interest in said corporation. In the event of the exercise of the option given to Second Party by the provisions of this paragraph and not otherwise, except as hereinbefore provided, that certain option given Second Party by paragraph 2 of this agreement shall immediately cease and terminate.

6. First Parties, and each of them, agree that they will continue in the employment of said Patterson-Ballagh Corporation and serve in executive capacities in connection with the business and affairs of said corporation for a period of not less than Two (2) years from the date hereof and at salaries not exceeding the rate of salaries now being paid them by said corporation for services rendered by them to said corporation and that they will cause the business of said corporation to be carried on in the same orderly and businesslike manner as at the present time. First Parties furthermore agree that so long as Second Party has

any right or rights under either paragraph 2 or paragraph 5 hereof, to purchase additional shares of the stock of said Patterson-Ballagh Corporation or in the event of the exercise by Second Party of either the option contained in said paragraph 2 or the option contained in said paragraph 5 hereof, First Parties will prevent said Patterson-Ballagh Corporation from declaring any dividends excepting out of the net profits of the business accruing subsequent to the date hereof and will prevent said Patterson-Ballagh Corporation from transferring any of its assets excepting in the ordinary and normal carrying on of its business and excepting in the declaration of dividends as aforesaid, provided, however, that this paragraph shall not be construed to in any manner prejudice the rights of Second Party as the owner of the Two Hundred and Fifty (250) shares of the capital stock of said Patterson-Ballagh Corporation as contemplated by paragraph 1 of this agreement.

7. Second Party agrees that so long as First Parties or their heirs shall own at least one-half (½) of the total issued and outstanding capital stock of the Patterson-Ballagh Corporation they shall have, and are hereby given, the right to elect and maintain in office a majority of the Board of Directors of said corporation and First Parties agree that Second Party so long as it owns any issued or outstanding capital stock of said corporation shall have the right to elect and maintain in office at least one director of said corporation, the parties hereto agreeing that before any of said par-

ties shall transfer any of the capital stock of said Patterson Ballagh Corporation to any party or parties other than the parties hereto, such party or parties so desiring to transfer such capital stock, shall offer such capital stock to the other party or parties hereto, upon terms as favorable as such party or parties so desiring to sell such capital stock are able to obtain from any outside party or parties, provided, however, that nothing in this paragraph contained, shall prevent either of the First Parties hereto or his heirs from transferring any of said shares to the other of the First Parties hereto or his heirs. Such party or parties hereto to whom such offer is so made shall have a period of Ninety (90) days in which to accept or reject such offer.

8. The covenants and agreements of the parties hereto as hereinbefore contained shall enure to and bind the heirs, executors, administrators and assigns of the respective parties hereto.

In Witness Whereof, the First Parties, each for himself, and Second Party by its officers thereunto authorized have set their hands and seals this 20th day of September, 1928.

(Signed) C. L. PATTERSON
(Signed) J. C. BALLAGH
Parties of the First Part

BYRON JACKSON PUMP CO.
(Signed) By ROBT. SCHURMAN
H. J. ELLEN
Secy.

[Endorsed]: Filed July 2, 1942.

Mr. Lamont: Attached to the complaint are three exhibits. The first is an exhibit dated August 5, 1941, a demand on the board of directors of Patterson-Ballagh to take some proceedings against the defendants.

Mr. Bednar: What date was that?

Mr. Lamont: That is August 5, 1941. I have the registry receipt, and that was sent to each of the other directors.

Mr. Bednar: Can we look at it during the noon hour?

Mr. Lamont: Surely. Also I would like to have you stipulate to Exhibit B—this may be admitted in the answer—a letter of August 8, 1941, written by Mr. Dulin to Mr. Miller, as president, urging him to take action.

Then Exhibit C was a notice to all the stockholders and a demand upon the majority stockholders to take some action. I am perfectly willing to have you check them, and if you find them—There is another matter at this time, before the noon recess, that you will probably stipulate to. There is named as a stockholder in the answer the Highland Investment Company. As a matter of fact, that was a company en- [35] tirely owned by Mr. Ballagh and his wife, was it not?

Mr. Bednar: I think so.

Mr. Lamont: In other words, during the time this litigation concerns itself with Byron Jackson Company owned 250 shares, and Mr. Miller owned 375 shares, and Mr. Ballagh, either in his own name or through Highland Investment Corporation,

owned 375 shares, which made up a total of 1,000 shares?

Mr. Bednar: That is correct.

Mr. Lamont: That is all of my documentary evidence. Shall I continue with the oral evidence now?

The Court: No. We will wait until two o'clock. The court will stand at recess until two o'clock.

(Thereupon, a recess was taken until 2:00 o'clock, p. m., of the same date.) [36]

Los Angeles, California
Thursday, July 2, 1942
2:00 o'Clock P. M.

The Court: You may proceed, gentlemen.

Mr. Lamont: I asked counsel to stipulate in regard to the serving or the sending of the exhibits to the complaint. Have you looked over these receipts, counsel?

Mr. Bednar: Yes. I examined them, and I will stipulate that Exhibit B attached to the complaint was received by Mr. Miller soon after this date.

Mr. Lamont: That is, August 8, 1941?

Mr. Bednar: That is right. And I will stipulate that Exhibit C attached to the complaint was received by all stockholders shortly after the date it bears.

Mr. Lamont: And that date was August 14, 1941?

Mr. Bednar: Yes.

Mr. Lamont: How about Exhibit A?

Mr. Bednar: You didn't ask about Exhibit A.

Mr. Lamont: Well, I meant to.

Mr. Bednar: In paragraph XI of the answer, I admit that the defendants "received a communication, purportedly from plaintiff, in words and figures as set forth in Exhibit A attached to the complaint."

Mr. Lamont: Can you make the same reply in regard to Mr. Burrell, who is also director, and also Mr. Armington, who is also a director? [37]

Mr. Bednar: Yes.

Mr. Lamont: I think possibly I had better read this to the court. Exhibit A is a demand upon the directors to take some action on behalf of the corporation.

"Byron Jackson Co., a Delaware corporation, and a stockholder in Patterson-Ballagh Corporation at the present time and at all times herein mentioned, hereby makes demand upon you to commence and prosecute a suit in the name of and on behalf of said Patterson-Ballagh Corporation against J. C. Ballagh and D. G. Miller on account of the following facts:

"1. That said Ballagh and one C. L. Patterson, at all times subsequent to September 20, 1928, and up to on or about February 15, 1939, were the principal stockholders of Patterson-Ballagh Corporation, owning and controlling three-fourths of the entire capital stock of said corporation, the remaining one-fourth of such capital stock being owned and controlled by the undersigned; that said Patterson during said time was the president and a director of said Patterson-Ballagh Corporation, and said Ballagh was secretary-treasurer and a di-

rector of said Patterson-Ballagh Corporation, and said Ballagh and said Patterson by said stock ownership controlled, [38] dominated, and directed each and every of the acts of said Patterson-Ballagh Corporation. That on or about February 15, 1939, said Patterson resigned as president and director of said corporation, and the entire stock owned by said Patterson in said Patterson-Ballagh Corporation was sold to one D. G. Miller by said Patterson; said Miller was thereupon elected president and a director of said corporation on said February 15, 1939, and since that date has been and still is the president and a director of said corporation. That since February 15, 1939, the said Ballagh and the said Miller have connived and cooperated in directing the affairs of said Patterson-Ballagh Corporation, and have at all times since said date dominated, controlled, and directed, and still do dominate, control, and direct each and every of the acts and doings of said Patterson-Ballagh Corporation.

"2. That as a part of a scheme and conspiracy said Ballagh and Miller, being in absolute control and domination of said corporation by reason of controlling three-fourths of the capital stock of said corporation and by reason of controlling the board of directors of said corporation, and over the protest of the undersigned, did pay to said Ballagh grossly excessive salaries [39] and compensation for services rendered said corporation, as follows."

And thereafter there are set forth the same allegations, in effect, as are set forth in the complaint.

Then continuing:

"The undersigned has at no time since February 15, 1939, received any dividends whatsoever from said Patterson-Ballagh Corporation, and the undersigned believes that said excessive salaries and compensation, as hereinbefore set forth, were determined by said Ballagh and said Miller in furtherance of the above-mentioned scheme and conspiracy, and with the purpose and intent of depriving the undersigned of dividends accruing or to accrue to the undersigned from the said Patterson-Ballagh Corporation and that the amounts of said salaries and compensation were neither fairly nor honestly determined by the said Ballagh and said Miller.

"That the undersigned hereby reiterates its demand upon the board of directors of said Patterson-Ballagh Corporation that suit be instituted and prosecuted by said Board in the name of and on behalf of the said corporation to collect from the said Ballagh and said Miller the amount of all excessive salaries and compensation." [40]

Then Exhibit B is a personal letter by Mr. Dulin, as president of the Byron Jackson Company, to Mr. Miller, as president of the Patterson-Ballagh Corporation, and Exhibit C is a demand, somewhat similar, but much shorter, upon the majority stockholders for some action.

Now, as a part of the minutes I introduced in evidence this morning is the repudiation of a royalty agreement. I put all four agreements in evidence. It is Exhibit A to your answer in the other suit. It is in the minutes, I understand. I thought it was set forth in the minute.

Mr. Bednar: The only letter set forth in the minutes is the letter from Mr. Burrell to Patterson-Ballagh Corporation, advising them of the action.

Mr. Lamont: I will offer this in evidence as Plaintiff's exhibit next in order. It is dated June 29, 1939, directed by Patterson-Ballagh Corporation to Byron Jackson Company. That is the repudiation of the agreement.

Mr. Bednar: It is perfectly agreeable with us for the notice to go in, but I have a right to check it.

Mr. Lamont: Your answer in the other suit sets it forth.

The Clerk: It will be Plaintiff's Exhibit 16.

PLAINTIFF'S EXHIBIT No. 16

June 29, 1939

Byron Jackson Co.
2150 East Slauson Ave.
Los Angeles, California

Gentlemen:

Please be referred to the following agreements:

1. Agreement dated September 20, 1928, between Byron Jackson Pump Company, therein called "Licensor," and Patterson-Ballagh Corporation, therein called "Licensee." We understand you are the successors of Byron Jackson Pump Company.

2. Agreement dated September 20, 1928, between Patterson-Ballagh Corporation, party of the first part, and Byron Jackson Pump Company, as party of the second part.

3. Instrument of assignment dated December 29, 1931, executed by Byron Jackson Company by which the latter sells, assigns, transfers and sets over to C. L. Patterson and J. C. Ballagh an undivided one-half interest in and to Letters Patent No. 1,619,728 (Hopkins patent) and an undivided one-half interest in and to the agreement first above mentioned.

4. Letter Agreement dated December 22, 1931, signed by Byron Jackson Company and approved December 29, 1931, by Patterson-Ballagh Corporation, J. C. Ballagh and C. L. Patterson.

You will please be advised that we hereby renounce and terminate said agreement dated September 20, 1928, first above mentioned; that we repudiate the license purported to be given by said agreement; that we hereby abandon any position as licensee under said agreement; that we hereby renounce any protection of said license agreement and that we hereby refuse to make any further payments as royalties or otherwise for said license or under said agreement, but without prejudice to the foregoing we are ready to pay and will pay royalties accrued and payable to date of receipt of this notice or July 1, 1939, whichever date is later. We do this for the reasons, among others, that the Letters Patent mentioned in said agreement and which are the basis of said agreement and license are, and each is, invalid and void and that there is a failure or lack of consideration for said license and agreement.

You are also advised that Byron Jackson Pump Company and Byron Jackson Company, as successor to Byron Jackson Pump Company, and its or their sub-licensees, are hereby released and discharged of all obligation to purchase from Patterson-Ballagh Corporation rubbers or cushions of any kind or nature used in connection with the manufacture, sale and use of Hopkins joints as set forth in the agreement designated as No. 2 above, and further that the undersigned corporation claims no rights or privileges under the Letter Agreement designated as No. 4 above, or in, to or under the so-called Hopkins patent No. 1,619,728.

This means also that any sub-licensees under agreements of license signed by Byron Jackson Pump Company or Byron Jackson Company and to which the undersigned is a party will not be required by us to purchase from the undersigned and to use only "Patterson-Ballagh Protectors" in the manufacture and sale of cushion joints for rotary drill pipes or for any other purpose, or otherwise be bound by the provisions of said sublicenses so far as we are concerned. Our action in respect to the agreements designated as No. 2 and No. 4 above is upon the ground, among others, that the patents mentioned and described in any of said agreements are, and each is, invalid and void and that there is a failure and lack of consideration for each and all of the agreements of

license hereby renounced or the performance of which is hereby released and discharged.

Respectfully yours,
PATTERSON-BALLAGH
CORPORATION
By D. G. MILLER

[Endorsed]: Filed July 2, 1942.

Mr. Lamont: Mr. Ballagh, will you take the stand? [41]

J. C. BALLAGH

called as a witness in behalf of the Plaintiff, being first duly sworn, testified as follows:

The Clerk: Please state your name.

The Witness: J. C. Ballagh.

Direct Examination

Q. By Mr. Lamont: Mr. Ballagh, what connection have you with the Patterson-Ballagh Corporation? A. Secretary and treasurer.

Q. How long have you been such?

A. Since 1928.

Q. In other words, since the organization of the company? A. Yes, sir.

Q. Who were the stockholders of the company at that time?

A. C. L. Patterson, Violet Patterson, and J. C. Ballagh.

(Testimony of J. C. Ballagh.)

Q. Violet Patterson is the wife of C. L. Patterson? A. She is.

Q. And what changes took place in stock ownership of that corporation since that time?

A. Byron Jackson Company bought 125 shares from C. L. Patterson and 125 shares from myself.

Q. And after Byron Jackson bought into the corporation what other changes took place, particularly so far as [42] Mr. Patterson's stock ownership was concerned?

A. Violet Patterson resigned, and Robert Sherman took her place on the board, with a transfer of one share of stock.

Q. I am asking about stock ownership. Mr. Patterson later on sold his shares, did he not?

A. Yes; he sold to Mr. Miller.

Q. On February 15, 1939? A. 1939.

Q. Along about that time. A. Yes, sir.

Q. And at that time he resigned from the board, did he not? A. Yes, sir.

Q. And Mr. Miller took his place on the board?

A. Yes, sir.

Q. What position did Mr. Patterson have with your company? A. President.

Q. And when Mr. Miller came on was your position changed at all? A. No.

Q. What position did Mr. Miller take?

A. President.

Q. What business is your company engaged in? I have particular reference now to the period from

(Testimony of J. C. Ballagh.)

February 15, [43] 1939, to the date of the commencement of this action on September 10, 1941.

A. The manufacture of oil field equipment, especially rubber items.

Q. It was especially a manufacturing business, was it not? A. Yes, sir.

Q. And what did it manufacture?

A. I wonder if I may get the catalog with the price lists. Casing protectors, stabilizers, special lip protectors, drill pipe stabilizers, Kelly sub protectors, installation tools and removal tools, slide plates, installation paste, hydraulic installation equipment, wire line guides, pipe wipers, safety swivel bail bumpers, Kelly wipers, flange grinders, wire line wipers, mud guns, mud gun nozzles, tubing protectors, sucker rod protectors, sucker rod wipers, traveling block bumpers, open hole steel clad tool joint protectors, vibration dampeners, and various mechanical rubber items made for customers to their specifications, and possibly a few other items of minor consequence that I haven't mentioned.

Q. Mr. Ballagh, what is the difference between a protector and a stabilizer?

A. A difference in the diameter and a difference in the length, and a difference in where it is used in the drilling of an oil well. [44]

Q. Well, they are, in effect, the same gadget, are they not, except for the size?

A. Except for their use and their size and length.

Q. What percentage of your business during

(Testimony of J. C. Ballagh.)

that period I just referred to consisted in the selling of protectors and stabilizers?

A. It varied in those three years, and I will have to get the figures, which I have available——

Q. That is perfectly satisfactory.

A. ——to show the volume.

Q. As a matter of fact, you can supply the figures. A. Yes.

Mr. Bednar: We are going to put this in evidence eventually.

Mr. Lamont: Put it in now, if you want to.

Mr. Bednar: All right. Defendants' Exhibit 1.

The Clerk: Defendants' Exhibit A.

Mr. Lamont: May I ask, whom was that prepared by?

Mr. Bednar: Mr. Ballagh.

Q. By Mr. Lamont: Mr. Ballagh, referring to this chart——

The Witness: I will have to have the other one, to get the quantity of protectors. There is another chart that gives that.

Mr. Bednar: Is this the one?

Mr. Lamont: I don't believe I have seen that. You were [45] kind enough to give me a copy of the other one. Referring to this chart, or these two charts—are you going to put this in evidence?

Mr. Bednar: Yes; I will offer this.

The Clerk: Defendants' Exhibit B.

Q. By Mr. Lamont: Referring to these two charts, Exhibit A and Exhibit B, Mr. Ballagh, what percentage of your business during the time that

(Testimony of J. C. Ballagh.)

I have specified consisted in the sale of protectors and stabilizers?

A. In 1931 the gross sales——

Q. I am not asking for 1931.

A. In 1939—I beg your pardon.

Q. 1939, 1940, and 1941.

A. In 1939 the gross sale of protectors and stabilizers was $261,741.70, from a gross total sale of $336,527.88. In the year 1940, protectors and stabilizers, gross sales were $233,758.23, from a total of $329,621.51. In the year 1941, protector sales, including stabilizers, were $245,012.22, from a gross total of $366,420.87.

Q. Mr. Ballagh, will you explain to the court what a protector is?

Mr. Lamont: I don't know whether you are going to put any protectors in evidence here or not.

Mr. Bednar: We have one here.

A. A casing protector is a continuous ring of rubber which has an inside diameter smaller than the inside diameter [46] of the drill pipe on which it is to operate. It is forced over the drill pipe and fuses itself upon the drill pipe by the resilience of the rubber, and in that position has a diameter that is larger than that of the tool joint, and acts as a bearing medium to prevent the wearing or whipping of the tool joint against the casing.

Mr. Lamont: Are you going to put these in evidence?

Mr. Bednar: Just for identification. We have got a lot of these.

(Testimony of J. C. Ballagh.)

Mr. Lamont: I wonder if they could be marked now for identification.

Mr. Bednar: Yes.

Mr. Lamont: The evidence would be more intelligible, I think.

Mr. Bednar: I have got some pictures here.

Mr. Lamont: There are apparently two——

Mr. Bednar: Mr. Ballagh, does that catalog have pictures of the protectors? A. Yes.

Mr. Bednar: I would prefer to offer them.

Mr. Lamont: That is perfectly satisfactory.

Mr. Bednar: You can offer these for identification. I just want to withdraw them at the end of the trial.

Mr. Lamont: Which are you offering as which? I am going to ask for the distinction between the two.

Mr. Bednar: We will offer the products themselves for [47] identification.

Mr. Lamont: How about the larger one in diameter?

Mr. Bednar: That is a non-lip protector. That will be Exhibit C. And the lipped protector will be Exhibit D, both of those for identification. And let us just offer the catalog in evidence.

Mr. Lamont: I am not stipulating to the contents of the catalog, but for the purpose of showing the pictures, that is perfectly satisfactory.

Mr. Bednar: For the purpose of showing the pictures, we will offer the catalog.

(Testimony of J. C. Ballagh.)

The Clerk: That will be Defendants' Exhibit E in evidence.

Q. By Mr. Lamont: What is the distinction, Mr. Ballagh, between the lip protector and the non-lip protector?

A. The non-lip protector is the protector that we made prior to 1939 and 1940, and is a protector that has a recess into the protector itself on the inside diameter, whereas the lip protector has a lip that extends out beyond the protector.

Q. Will you point out to the court where the lip is.

A. The protector that we had been making has a recess, and the new design——

The Court: This is the new one?

A. That is the new design, yes, sir. [48]

Q. By Mr. Lamont: Is there any other distinction between the two, Mr. Ballagh?

A. Not in construction, no, sir.

Q. You have given the figures as to gross sales, apparently, of these two gadgets together?

A. Yes, sir.

Q. What was the next biggest item constituting the gross sales?

A. During 1939 the wire line guide had a gross sale of $33,525.18.

Q. Out of a total of gross sales of apparently $336,527.88? A. Yes, sir.

Q. And how about 1940?

A. In 1940 the wire line guide gross sales were $32,694.98.

(Testimony of J. C. Ballagh.)

Q. And 1941?

A. In 1941 the drill pipe wipers had a gross sale of $43,862.20, from the total given.

Q. What was your next largest product in the way of gross sales?

A. In 1939 the drill pipe wipers, where the volume was $12,296.

Q. How about 1940?

A. In 1940, the drill pipe wipers was $30,189.50, from the total given. And in 1941 the wire line guide was [49] $34,996.84, from the total given for that year.

Q. Mr. Dulin points out that probably in this table you have used the term "wipers," and it should have been "wire line guides." You are taking all of that, are you not, from Defendants' Exhibit A?

A. I think I am right on it. I will confirm those figures; I will check them back.

Q. We thought you misspoke.

Mr. Bednar: You are asking which was the next largest in sales, and they differed in 1939 and '40—in 1939 and 1940 the next item was line guides, and in '41 it was pipe wipers.

Mr. Lamont: Let us clear it up in this manner. Practically all of your gross sales during this period consisted of protectors, wire line guides, and pipe wipers; is that not a fact?

A. No. In 1939 we sold $11,633.33 of swivel protectors.

Q. Out of the total——

(Testimony of J. C. Ballagh.)

A. $5,983.51 of mud guns, and $5,426.70 of hydraulic equipment; $3,294 of tubing protectors; and about $2,000 of other miscellaneous items.

Q. But the sales of those other articles were minor in comparison with the three that I have mentioned; isn't that true? It is perfectly obvious from the exhibit.

Mr. Bednar: I think the exhibit shows that. [50]

Q. By Mr. Lamont: One further question I would like to ask with regard to these charts. I am not familiar with Exhibit B. Will you explain what that shows.

A. Exhibit B is a graphic illustration of the distribution of our protector sales by those that were installed with a hydraulic machine and those that were sold in which the lip was a part.

Q. In other words, between C and D for identification—that is what I am not certain of.

A. The gross total sales, for instance, in 1940, for example, were divided into Mid-Continent sales, California sales, export and miscellaneous United States sales outside of this area, and I have gone through the files and I have determined that 25 per cent of the sales of all casing protectors in the Mid-Continent were installed with hydraulic machines, 75 per cent in California, and 10 per cent in miscellaneous fields, and none for export.

Q. The term "hydraulic" means the non-lip protector; is that correct? A. No.

Q. That is what I am not clear on.

A. I was trying to illustrate the gross sales of

(Testimony of J. C. Ballagh.)

protectors in terms of the two types sold, the lip protectors, and those are installed by hydraulic methods.

Q. Let me ask you this. Were any of the protectors installed by hydraulic methods lip proectors?

[51]

A. Oh, yes.

Q. But the percentage is not shown here, apparently?

A. No. We have no way of determining for our records as to which lip protectors were installed with a hydraulic machine.

Mr. Bednar: Let us take, for example, Mr. Ballagh, the year 1940, and the column headed "hydraulic." That column includes all protectors, lip and non-lip, does it not? A. Yes.

Mr. Bednar: And a portion of it, the portion of that column shown in blue, for example, 25 per cent in the Mid-Continent and 75 per cent in California, indicates the percentage of all protectors, lip protectors and non-lip protectors, installed by the hydraulic method? A. Yes.

Q. By Mr. Lamont: In other words, in the left-hand column of each of those four columns?

A. The sale of the lip protector and the use of the hydraulic applicator.

Mr. Bednar: Taking the year 1940, and directing your attention to the column headed "Lip Pro"—— A. Yes.

Mr. Bednar: You have certain areas there colored in yellow and others in white. I will ask

(Testimony of J. C. Ballagh.)

you whether or not that doesn't mean that of all protectors, both lip and non-lip protectors, installed in 1940, 25 per cent were lip pro- [52] tectors.

A. Yes, sir.

Q. And the white area represents the non-lip protectors? A. Yes, sir.

Mr. Bednar: In other words, the purpose of this chart is to indicate the progress of lip protectors and the use of hydraulic applicators in installing our protectors? A. Yes, sir.

Q. By Mr. Lamont: How else are protectors installed other than by hydraulic applicators?

A. They are installed by the old original manually operated applicator, in which there is no hydraulic power applied.

Q. Mr. Ballagh, where were these protectors and the other articles you have mentioned manufactured?

A. At the Patterson-Ballagh factory at 1900 East 65th Street, Los Angeles.

Q. Were they manufactured any other place?

A. No, sir.

Q. In other words, that was the sole manufacturing establishment?

A. That is true, for protectors.

Q. I believe you did, however, have a repair shop in Houston, was it? A. Yes, sir.

Q. Texas? [53] A. Yes, sir.

Q. And outside of that, apparently all you had were certain sales agencies in which you displayed——

(Testimony of J. C. Ballagh.)

A. We had service stations at a number of points. The manufacturing was done entirely in California, and some assembling done in Houston.

Q. How many employees did you employ during this period of time?

A. During 1939 and 1940 and 1941 the average was slightly over 40.

Q. Slightly over 40? A. Yes, sir.

Q. I believe in your deposition you tesitfied that you ranged from 25 to 40.

A. I did, but I found that I was low by a few.

Q. That included all of your employees?

A. Yes, sir.

Q. During this period did you have any financial problems as far as the company was concerned?

A. No, sir.

Q. During this period did your duties in any way change? Did the work that you did for the company in any way change?

A. I don't believe that they changed materially, except that during 1939 and 1940 I spent more time in the factory, because of Mr. Miller coming into the firm. [54]

Q. Mr. Miller took Mr. Patterson's place, did he not? A. Yes, sir.

Q. He was supposed to carry on Mr. Patterson's duties? A. Yes, sir.

Q. And until he became acquianted with the business, you may have had a few of those duties to perform; is that correct? A. Yes, sir.

Q. Otherwise there was no change?

(Testimony of J. C. Ballagh.)

A. Practically none.

Q. During this period that Mr. Miller worked for the company, did they change in any material respect?

A. He carried on approximately the same duties that Mr. Patterson had.

Q. Did they remain the same through these years?

A. I would say virtually the same, yes, sir.

Q. You said you were secretary and treasurer?

A. Yes, sir.

Q. Did you keep the minutes of the corporation during this period?

A. No. I kept a few notes on them, and Mr. Burrell wrote up the minutes.

Q. But you didn't yourself write up the minutes?

A. No, I didn't.

Q. Did you keep the books? A. No, sir.

[55]

Q. Yourself? A. No, sir.

Q. You had a man to keep the books?

A. Yes, sir.

Q. Were they under your guidance or not?

A. Yes. They were under my office, as secretary and treasurer.

Q. But you didn't keep them yourself?

A. No, sir.

Q. Now, apparently on February 15, 1939, Mr. Miller became a director and president of the company? A. Yes, sir.

Q. How long had you known Mr. Miller?

(Testimony of J. C. Ballagh.)

A. I first met him about 34 years ago. I first met him——

Q. In other words, you have known him for a long time?

A. No. I went to the same college, but it was about 20 years after I had graduated before I saw him again.

Q. How did he happen to buy in the business? Did he go to you or did you go to him?

A. He came to me.

Q. And you put him in touch with Mr. Patterson, apparently? A. Yes, sir.

Q. And he bought out Mr. Patterson's stock? [56]

A. Yes, sir.

Q. How did you know that Mr. Patterson's stock was for sale?

A. I talked with Mr. Patterson on a number of occasions regarding it.

Q. How did Mr. Miller know that Mr. Patterson's stock was for sale?

A. I introduced Mr. Miller to Mr. Patterson.

Q. Did he know that stock was for sale before he came to you or not? A. Mr. Miller?

Q. Yes. A. No.

Q. Who was Mr. Armington? Apparently he went on the board of directors.

A. Mr. Armington is the man that does our engineering work, engineering and specifications, and assisting in machine design and costs and field service.

(Testimony of J. C. Ballagh.)

Q. How long had he been employed by the company?

A. He has been with us, I think, about 12 years.

Q. Prior to this time?

A. Yes, sir.—about 12 years from now.

Q. How much did you pay him?

Mr. Bednar: When?

Q. By Mr. Lamont: Beginning January 1, 1939.

A. We were paying him $225 a month for part of his [57] time.

Q. I note from the evidence already introduced that Mr. Burrell became a director of your company on June 27, 1939. A. Yes.

Q. Who is Mr. Burrell?

A. Mr. Burrell is one of the firm of Musick and Burrell.

Q. Had you employed him prior to that time in any capacity as an attorney?

A. He had worked on a case for Patterson-Ballagh Corporation about six or seven years ago.

Q. Did he have anything to do with putting this transfer of stock through from Patterson to Miller? A. Yes. He prepared the option.

Q. He was, in effect, the attorney for your company at the time he went on the board?

A. No, not at that time.

Q. But he became such, didn't he?

A. Yes, sir.

Q. And when did he become such?

A. I think two or three months after he went on the board.

(Testimony of J. C. Ballagh.)

Q. Who suggested that Mr. Burrell go on the board? A. I think I did.

Q. Who suggested that Mr. Armington go on the board? [58]

A. I don't remember. It may have been Mr. Elliott, but I can't recall.

Q. Let me ask you this: Prior to your meeting February 15, 1939, did you ever discuss with Mr. Dulin or any representative of the Byron Jackson Company about Mr. Armington going on the board?

A. I don't recall that I did.

Q. I will ask you the same question with regard to Mr. Burrell, as to the meeting of June 27, 1939.

A. I don't recall that I did.

Q. Who outlined the policies of your company?

A. During——

Q. Who did during this period?

A. During 1939?

Q. 1939, 1940, and 1941.

A. They were outlined jointly by Mr. Miller and myself.

Q. Mr. Miller, as president, and you, as secretary?

A. Yes, subject to the action of the board.

Q. On August 22, 1939, apparently your salary was raised, was it not?

A. Apparently so, if it is in those records. I don't remember the date.

Q. That shows on the records, I believe.

Mr. Bednar: That shows in the minutes.

(Testimony of J. C. Ballagh.)

Q. By Mr. Lamont: What had been your salary prior to [59] that time?

A. I will have to look at the minute and that salary record, if I may. On August 15th I drew a salary of $1,000 a month, I think, according to this.

Q. As a matter of fact, that was a raise, was it not, of $4,000, payable quarterly? A. Yes, sir.

Q. And, as a matter of fact, you had been drawing that raise before it was approved by the board, had you not, or even presented to the board?

A. Yes, sir.

Q. In other words, you dated that raise back of the board meeting to March 1st of that year; is that not true? A. Yes, sir.

Q. Mr. Dulin was not present at that meeting?

A. No, sir. The minutes show that he was absent on that day.

Q. Before that raise was made, with whom did you discuss the matter of your increase in salary?

A. With Mr. Miller.

Q. With anyone else?

A. I can't recall whether I discussed it with Mr. Armington or not, but I discussed it with Mr. Burrell.

Q. Did you discuss it with Mr. Dulin?

A. No, sir, I don't recall that I did.

Q. Apparently also on March 18, 1940, your salary was [60] raised, was it not?

A. Yes, sir.

Q. What was it raised to?

(Testimony of J. C. Ballagh.)

A. It was raised to $2,000 a month.

Q. With whom did you discuss that raise prior to that time?

A. Mr. Miller and Mr. Burrell, and I am not sure whether I did with Mr. Armington or not.

Q. Did you discuss it with Mr. Dulin?

A. I don't recall.

Q. You wouldn't say that you did?

A. I wouldn't say that I did.

Q. He was present at that meeting, was he not?

A. Yes.

Q. And voted in the negative with respect to your raise? A. Yes, sir.

Mr. Lamont: At this time I would like to read what the record shows, the corporate minutes, in regard to this resolution increasing the salary to $2,000 a month:

> "Director Dulin stated that he objected most strenuously to the suggested increase and expressed himself as feeling that the same was entirely unwarranted and should not be put into effect under any conditions until the corporation was paying satisfactory dividends to its shareholders." [61]

Q. Now, Mr. Ballagh, on November 29, 1940, you again increased your salary or paid yourself a bonus, did you not?

A. Additional compensation for the year end.

Q. Additional compensation? A. Yes.

Q. How much did that amount to?

(Testimony of J. C. Ballagh.)

A. $4,166.66.

Q. And at the same time Mr. Miller increased his compensation? A. Yes, sir.

Q. By how much? A. $2,750.

Q. Did you discuss either of these items of raises with Mr. Dulin prior to that time?

A. No, sir, I don't recall that I did.

Q. In discussing with Mr. Miller these raises did you discuss with him the profits of the company? A. Yes.

Q. Did you take them into consideration in making these three raises? A. Yes, sir.

Q. As a matter of fact, the profits of the company were increasing in proportion to the raises, were they?

A. The books are explanatory. You have all the statements.

Q. Do you recall at the present time? [62]

A. I don't think they did. I haven't the figures.

Q. Did you discuss that element with Mr. Miller? A. No, sir.

Q. Or Mr. Burrell? A. No.

Q. Do you recall whether or not Mr. Dulin was present during that part of the meeting when you voted yourself that additional compensation or the additional bonus?

Mr. Bednar: The minutes don't indicate that Mr. Dulin was there.

Mr. Lamont: I think that is true, that he was not there. I am asking him, and on his last extra

(Testimony of J. C. Ballagh.)

compensation, whether Mr. Dulin was present at the time the compensation was voted.

The Witness: The minutes show that he was absent.

Q. In the discussions with Mr. Miller and Mr. Burrell and Mr. Armington with regard to increases or extra compensation, did you talk about the non-payment of dividends?

A. I think we did. I can't recall specifically.

Q. Did you take them into consideration in raising your salary?

A. I think they were taken into consideration, yes, sir.

Q. You hadn't paid any dividends since 1938, had you, the summer of 1938?

Mr. Bednar: I object to that as already in evidence. [63] I think the record shows.

Mr. Lamont: I think that is probably true. In the summer of 1938 I think the record showed dividends.

Q. By Mr. Lamont: After the end of June 1939 you paid no more royalties, did you, under your contractual arrangement with Byron Jackson, numbered Exhibit 15? I will show you that.

A. I think in the exhibit there is a list of dividends and the dates and the check numbers, which gives the date of the last check paid.

Q. As a matter of fact, that was in the summer of 1939, was it not?

A. I can tell if you will hand me that dividend

(Testimony of J. C. Ballagh.)

Mr. Bednar: This shows dividends and royalty payments.

Q. By Mr. Lamont: Referring to this chart which I now show you——

Mr. Lamont: Are you going to put that in evidence?

Mr. Bednar: Yes.

Mr. Lamont: I would prefer that you offer it now.

Mr. Bednar: I will offer it now, then.

The Clerk: That will be Defendants' Exhibit F in evidence.

Q. By Mr. Lamont: Referring to Defendants' Exhibit F, that was prepared by you, was it not?

A. Yes, sir. [64]

Q. And it shows, does it not, that royalties and dividends stopped short in the middle of 1939; is that not correct?

A. This shows the final payment made prior to January 1, 1940, the exact date of which I haven't got.

Mr. Lamont: Let us get at it this way. I presume you will stipulate that there were no more royalties paid after the serving of notice of cancellation of the contract, and that there were no dividends paid after the middle of 1939?

Mr. Bednar: That is correct.

Q. By Mr. Lamont: How much had you been paying just prior to that time, and by "that time" I mean the summer of 1939, to Byron Jackson, on

(Testimony of J. C. Ballagh.)

account of royalties under the agreement with them?

A. May I have tabulation showing the dividends paid?

Mr. Bednar: I understand you asked about royalties?

Mr. Lamont: Yes, royalties.

The Witness: Royalties.

Mr. Bednar: I am afraid that is not in evidence.

Mr. Lamont: My understanding is that Byron Jackson were paid about $3,000 a year at that time, prior to that.

A. During 1939, up to and including 7/25, they received a total of $5,815.75. In the year of 1938 they received $11,816.25. During 1937 they received $12,458.75. And during 1936 they received $9,841.50. Do you wish it [65] prior to that time?

Q. No. As a matter of fact, one-half of each of those sums you have mentioned as being received by Byron Jackson was paid, under the contractual arrangement, to you and Mr. Patterson, was it not?

A. Yes, sir.

Q. Now, on November 29, 1940, you testified as to the raise of your compensation, and also the raise in Mr. Miller's compensation. That is correct, is it not? A. August, 1940?

Q. Yes.

Mr. Bednar: I think you said November, 1940.

Q. By Mr. Lamont: November, 1940—November 29, 1940. A. Yes, sir.

Q. And prior to that time I believe you testified

(Testimony of J. C. Ballagh.)

that you had talked with Mr. Miller in regard to your raise in compensation? A. Yes, sir.

Q. And you had also talked to him prior to that time in regard to his own raise? A. Yes, sir.

Q. As a matter of fact, they went hand in hand, did they not?

Mr. Bednar: I object to that.

Mr. Lamont: He is one of the defendants in the action. [66]

The Court: I know, but "hand in hand"——

Q. By Mr. Lamont: They were considered at the same time and in the same conversation, were they not?

A. During the same period of our discussion, of the conversation.

Q. And put up to the directors of the same board? A. Yes, sir.

Q. Now, why didn't you pay dividends after the summer of 1939?

A. Mr. Miller said that he would not approve any dividends as long as we had a suit pending in which it was necessary for us to set up a fund for the payment of potential loss of the suit we were having with Byron Jackson.

Q. In other words, you set up a reserve?

A. Yes, sir; we set up a reserve. And also because things were getting critical in the war, and we were planning on doing some expansion, trying to get into war work, and he said he didn't consider our cash on hand adequate to pay dividends.

(Testimony of J. C. Ballagh.)

Q. How much of a reserve did you set up from then on?

A. We set up the full sum of the amount that was potentially payable under the contract in cash.

Q. How much was that?

A. I think it was approximately $23,000, up to the first of 1942.

Q. How much on a yearly basis? [67]

A. I would have to get it year by year.

Mr. Bednar: The Pennington audits show this, that on March 29, 1940, Mr. Pennington's report indicates that at that time, for the preceding part, or for the last half, rather, of 1939, a reserve amounting to $4,799.25 was set up. Mr. Pennington's report dated February 10, 1941, indicates that for the year 1940 a reserve of $13,581.75 was set up. Mr. Pennington's report dated December 29, 1941, indicates that for the year 1941 a reserve was set up of $22,469.25. And I think that that reserve accumulates from year to year. That last figure is the total reserve as of November 30, 1941.

Mr. Lamont: How much is that figure?

Mr. Bednar: $22,469.25.

Q. By Mr. Lamont: Mr. Ballagh, after setting up these reserves, there were still profits left, were there not, which could have been paid out in dividends? A. Yes, sir.

Q. In raising your salary during this period did you take into consideration the possibility of war? A. Yes, sir.

(Testimony of J. C. Ballagh.)

Q. In the same way you took into consideration the payment of dividends or the non-payment of dividends? A. Yes, sir.

Q. But you raised the salaries, but you didn't pay [68] dividends; isn't that correct?

A. Yes, sir.

Q. In the monthly statement which was introduced in evidence, did you set up any reserve for taxes?

A. I don't think there were in the monthly statements. I can't recall, but I don't think we set up a monthly tax reserve.

Q. As a matter of fact, there appears in your minutes, does there not, a resolution to the effect that monthly reserves should have been set up by the treasurer of the company for taxes?

Mr. Bednar: The minutes speak for themselves. We will see. Could you point out that resolution to me?

(Discussion between counsel off the record.)

Q. By Mr. Lamont: Let me ask you this, Mr. Ballagh. The complaint has attached to it three exhibits, a demand upon the directors that the company take action against you and Mr. Miller. You recall that demand, do you not? A. Yes, sir.

Q. What did you do when you received that demand? A. Sent it to Mr. Burrell.

Q. Did you do anything else?

A. I can't recall.

(Testimony of J. C. Ballagh.)

Q. You didn't hold any directors meeting, did you?

A. Not that I recall—none except what is shown on our minutes. [69]

Q. Were you familiar with the letter that Mr. Dulin wrote to Mr. Miller, as president of the company, attached to the complaint as Exhibit A?

A. I think I saw it, yes, sir.

Q. What was done, if anything, upon receipt of that letter?

A. I think Mr. Miller sent it to Mr. Burrell.

Q. That is all that you know that was done?

A. Yes, sir.

Q. Exhibit B to the complaint is a demand upon the stockholders. Upon receipt of that demand what action did either you or Mr. Miller take?

A. I sent mine to Mr. Burrell.

Q. Did you take any further action?

A. No, sir.

Q. Did you discuss this matter with Mr. Burrell at that time? A. I think I did, yes.

Q. But you don't recall of ever having discussed it in any meeting of the board of directors?

A. I don't recall that I did.

Mr. Lamont: I will refer to the minutes of September 27, 1938. Apparently they contain this statement:

> "The next question was the matter of setting aside monthly reserves to cover the estimated income tax payments. It was moved by Mr. Elliot, [70] seconded by Mr. Rennie, that cash

(Testimony of J. C. Ballagh.)

equal to the book reserve be deposited in the fund account at the Security First National Bank to cover the estimated income tax liability on monthly earnings. Motion unanimously carried.''

Take the witness.

Mr. Bednar: No cross examination. [71]

Mr. Lamont: Mr. Miller, will you take the stand?

The Court: We might have a brief recess before Mr. Miller is sworn.

(Short recess.)

Mr. Lamont: I would like to put Mr. Ballagh back on the stand for a few more questions.

The Court: Very well.

J. C. BALLAGH, recalled

Direct Examination, resumed

By Mr. Lamont:

Q. Mr. Ballagh, during the course of your deposition taken in this matter, you testified, I believe, that during this period, I believe 1939, through 1939, 1940 and up to September 10, 1941, you did some work in regard to inventions; is that correct?

A. Yes, sir.

Q. As to which particular products was that work?

A. May I have the price list? On direct inven-

(Testimony of J. C. Ballagh.)

tions of mine I worked on the pipe wipers, tubing protectors, and box style sucker rod protectors, on the lip protectors, on the hydraulic applicators, on the Kelly wipers, mud gun, manifolds, on the traveling block bumper, on the vibration damper, being the main items during that period.

Q. In giving that testimony I take it you are referring to Defendants' A? [72]

A. Yes, sir.

Q. That is correct, is it not? A. Yes, sir.

Q. Now, apparently during the year 1939 the only protectors you sold were without lips; that is correct, is it not?

A. Yes, sir, except there was one experimental order sold in 1939 in the Mid-Continent. I didn't show it here, because it would hardly show on here. It was our first experimental order, and I think nothing except a few scattered experimental ones were installed then.

Q. When did you start working on that device?

A. On the lip protector?

Q. Yes. A. I think during 1939.

Q. You don't recall about what time?

A. It was during the summer or fall of 1939.

Q. But the only difference between the protectors theretofore manufactured and this lip protector was as you pointed out to the Court in your prior testimony; that is true, is it not?

A. Yes, sir, the construction.

Q. Did you patent this protector?

A. No, sir, not yet.

(Testimony of J. C. Ballagh.)

Q. Have you filed any application to patent it?

A. Yes, sir. [73]

Q. When did you file that?

A. That was filed in September, 1940.

Q. Have you a copy of your application?

A. Yes, sir.

Q. May I see it? A. Yes, sir.

Q. Referring to the diagram which you have handed to me, and referring to the figures numbered 1, 2, 3 and 4, will you explain to the Court what the distinction between those figures is?

A. I can best illustrate it in connection with the protector itself. This is the old original protector, as it has been made for about the past thirteen years, and it has a groove in each end on the inside diameter, so that they can be installed. The lip protector has no groove, and has a lip extending out from the protector, so that when it is installed on the pipe it has no recess; it has no recess in the space between the protector and the pipe.

Q. Mr. Ballagh, has there been any Patent Office action on that application?

A. Not as far as I know.

Q. As far as you know, no claims have been allowed?

A. As far as I know, not to date. It is in the hands of Lyon & Lyon, who are prosecuting it.

Q. During that period of time did you give gross profiits derived by your company from the sale of protectors [74] and stabilizers, making no distinction between lip protectors and the other type?

(Testimony of J. C. Ballagh.)

Mr. Bednar: You mean cost of manufacture?

Mr. Lamont: No—gross profits from both these devices during that period of time, 1939, 1940 and 1941.

Mr. Bednar: I object to the question until you define what you mean by "gross profits." Do you mean the sales price, less the cost of manufacturing the article itself?

Mr. Lamont: Let us have him give that first.

The Witness: What is the question?

Mr. Bednar: What is the average sale price on these protectors and what is the approximate cost of manufacture?

A. It would average, of all sizes, about $8.00, as a rough estimate. There are more than 100 different sizes, and it is rather a rough estimate as to the average of all sizes.

Q. How about the 4½-inch size?

Mr. Bednar: Is that $8.00 figure the cost or the selling price?

A. That is the average selling price.

Q. By Mr. Lamont: What is the cost of manufacturing?

A. Labor and material on that would be approximately $2.00.

Q. You gave the average. Now, will you confine yourself to the 4½-inch protector?

A. The 4½—we have nine sizes of 4½ protectors, and [75] we have about the same number of sizes of——

Q. Well, what is the average for your 4½?

(Testimony of J. C. Ballagh.)

A. They run from $10 to $19, list, with a deduction of 40 percent in California.

Q. Which are principally sold, which items? I believe in your price list you distinguish by code names, and also by weight in pounds.

A. The protector that sells for $13.50 would probably have the most sale in quantity in the Mid-Continent area, and in the California area the protector that lists at $10.50 would be the most popular size; and for export the most sold size in 4½ would be one that lists at $8.00.

Q. How does the manufacturing cost vary as to those items you have just mentioned?

A. Well, based on poundage, they all run about the same per pound. There is quite a variation in weights in the various sizes, and the pound selling price would be fairly close.

Q. Are there any competitive devices on the market? A. Yes, sir.

Q. There were during this period?

A. Yes, sir.

Q. What were they?

A. There was a protector called the Bettis Protector, made by the Bettis Rubber Company. There was a protector called the Grisly Protector, made by the Grisly Manufacturing [76] Company. There was a protector called the O. K. Protector, made in Houston, by the O. K. Manufacturing Company. And there was a protector made in Oklahoma by a man by the name of Howard. I think he calls it the

(Testimony of J. C. Ballagh.)

Howard Protector, if I am not mistaken. It is a small company.

Q. In the main, how do these competitors' devices differ from the protectors and the stabilizers manufactured by the Patterson-Ballagh Company?

A. Well, they are similar in their construction. None of them, however, have the lip.

Q. Now, Mr. Ballagh, coming to your Exhibit A, apparently, from looking at that exhibit, you are claiming some invention as to pipe wipers?

A. Yes, sir.

Q. What was that invention?

Mr. Bednar: I have a copy of the patent.

A. I have one of the devices here. I will illustrate.

Q. When did you start your work in regard to this pipe wiper patent?

A. In 1938 I started working on the design.

Q. When did you first start to sell this device?

A. I think our first sales were made in 1938.

Mr. Lamont: I would like to offer this patent in evidence. If you are going to put this elaborate chart in evidence, will you do it at the present time?

Mr. Bednar: Yes, we will. [77]

A. The first sales were made in 1938.

Mr. Bednar: Can we get a number on these exhibits before we go any further?

The Court: This chart will be Defendants' Exhibit G.

(Testimony of J. C. Ballagh.)

Mr. Bednar: The pipe wiper patent is what?

The Clerk: May I mark that, please? That patent will be Defendants' Exhibit H.

The Witness: Pardon me. I think I told you 1938. The first sales on that were during 1939, according to this record, instead of 1938.

Q. By Mr. Lamont: This chart, Defandants' Exhibit G, would show that?

A. Yes, sir. There may have been one or two experimental ones prior to that.

Q. Prior to 1939? A. Yes.

Mr. Bednar: I would like to have him explain what a pipe wiper is.

Mr. Lamont: I would be very glad to have him do it.

A. I have a small model in my portfolio. It is in one of the pockets. This full size is rather heavy. This is a wiper that wipes the mud from a drill pipe in an oil well or oil from tubing from a pumping well. It is put over the drill pipe and beneath the rotary table, and the drill pipe is pulled on up through, and it wipes the mud off. It is reenforced with steel, covered with rubber, made [78] with various sizes of holes to fit various size drill pipe or tubing.

Mr. Bednar: Do you have different sized pipe wipers?

A. Different size pipe wipers. There are six different sizes of pipe wipers.

Q. By Mr. Lamont: During this period, Mr.

(Testimony of J. C. Ballagh.)

Ballagh, were there any competitive devices on the market?

A. Yes, sir.

Q. What were they?

A. One was called the Meaderis Dri-Pipe Wiper.

Q. Any others?

A. As far as I know, that was the only one on the market at that time.

Q. Was that on the market before your device went on the market or not?

A. As far as I know, not. I never saw one until a considerable time after we had started marketing ours.

Q. How did it differ from your device?

A. Well, they made three or four designs, and at the present time, as far as I know, there is none being sold. I haven't seen them for at least a year. Theirs was made without any reenforcing, just canvas on the edge, and the first ones they had made had an aluminum housing on the outside, and then they had a brass housing, and then they went to the canvas webbing, and, as far as I know, they have discontinued the manufacture of them at the present time. [79]

Mr. Lamont: I think that will be all. You have no cross examination?

Mr. Bednar: No cross examination.

Mr. Lamont: All right. Mr. Miller, will you take the stand? [80]

DE MONT G. MILLER

called as a witness on behalf of the plaintiff, being first duly sworn, testified as follows:

The Clerk: Please state your name.

The Witness: De Mont George Miller.

Direct Examination

By Mr. Lamont:

Q. Mr. Miller, what position do you hold with Patterson-Ballagh Corporation?

A. President and manager of the corporation.

Q. How long have you been such?

A. Since February 15, 1939.

Q. What work did you carry on as such president and manager?

A. Manager of the factory, looked after the financial end of it, and purchasing.

Q. Did you do any inventing?

A. Yes, sir.

Q. What items?

A. I received a patent on two different line wipers.

Q. Anything else?

A. I believe I received two claims on a steel clad open hole stabilizer, steel clad protector; they call it a steel clad protector.

Q. Protector? [81]

A. Steel clad protector.

Q. Any others?

A. I have just put in an application on a rod protector, rod style, we call it.

Q. Any others?

(Testimony of DeMont G. Miller.)

A. And an affidavit on a rod wiper.

Q. Any others? A. That is all.

Q. Which of these items, if any, have been patented? A. The two line wipers.

Q. What? A. Line wipers.

Q. When did that patent issue?

Mr. Bednar: I have a copy of it.

A. He has got it.

Q. By Mr. Lamont: Have any other of these items been patented?

A. We haven't received the patents yet.

Q. Have you filed applications on the others?

A. I filed an application on the steel clad. That is the one I stated we received a couple of claims on. We have been notified by the attorneys that they have been allowed two claims.

Q. How about the rod style?

A. An application has just been written up by the attorneys. It hasn't been filed yet. [82]

Q. How about the rod wipers?

A. There has been only an affidavit put in.

Mr. Lamont: I would like to offer in evidence the patent on the line wiping device.

Mr. Bednar: There are two patents.

Mr. Lamont: Did you give me both of them?

Mr. Bednar: Yes.

Mr. Lamont: I will offer both of them as one exhibit, A and B.

The Clerk: They will be Plaintiff's Exhibits 17-A and 17-B.

(Testimony of DeMont G. Miller.)

Q. By Mr. Lamont: When did you start working on the line wipers?

A. Approximately a year before the patents issued.

Q. How about the steel clad protectors?

A. The patent attorneys have had that—at least, we filed application probably a year ago.

Q. When did you start your work?

A. I beg your pardon?

Q. When did you start in working on that device? A. Probably two years ago.

Q. How about the rod style protector?

A. I made an affidavit on that just about a year ago.

Q. How long prior to that time did you start working on it?

A. Probably a few weeks. [83]

Q. How about the rod wiper?

A. That is a guess, too. I could find out those dates from the affidavits, if you would like to have them.

Q. How long ago was that?

A. Probably a year ago.

Q. Coming to the line wipers, were there, during this period, any competitive devices on the market?

A. Yes, sir.

Q. What were they?

A. I only know of one, the Ratigan.

Q. How did that differ from your device?

(Testimony of DeMont G. Miller.)

Mr. Bednar: You might have him explain this with the model.

Mr. Lamont: All right.

A. This device is made in the form of a propeller with a lot of holes through it. The hole starts on each end, and the device is wrapped around the line, and, because of the resilience of the rubber it continues to stay tight and tightens up as you pull on it, until a hole is worn through bigger than the line, and then they buy another one. This particular device is so designed that whatever is on the end of it—a pump or tool joint—when it hits it it pops off by itself. Do you want me to explain this Ratigan device?

Mr. Lamont: Mr. Bednar, you have been very liberal in supplying charts. Have you any charts which show the [84] percentage of sales of these articles compared with the gross sales of the company?

Mr. Bednar: On Defendants' Exhibit A the yellow refers to small sales.

Mr. Lamont: In other words, it would appear, then, in 1939, that there were no sales of any of these articles?

Mr. Bednar: If so, they were inconsequential and wouldn't show on the chart.

Mr. Lamont: In 1940, the total would be how much?

Mr. Bednar: Well, as I read it, line wiper refills, $162.04; wire line wipers, $1952.40; Universal sucker rod wipers, $174.50. In 1941 there were sales of the open hole tool joint protector of $597.29; the wire

(Testimony of DeMont G. Miller.)

line wiper refills $3038.40; wire line wipers, $2250.60; and Universal rod wipers, $239.70.

Mr. Lamont: You have been reading, Counsel, apparently from Defendants' Exhibit A?

Mr. Bednar: Yes. We have one of the steel clad protectors.

Mr. Lamont: That is perfectly satisfactory.

Mr. Bednar: Before we go into this, you might explain the other wire line wiper.

Mr. Lamont: Just before that, referring to the figures you gave, they were out of a total of $336,527 for the year 1939, and $329,621 for the year 1940; and for the year 1941, $366,420? [85]

Mr. Bednar: The chart shows that. Mr. Miller, will you explain your other wire line wiper?

A. There were objections to price in the first line wiper by some of the customers, so this one was designed, with a similar device as to core, with a steel shield designed so that when the pump barrel, or whatever hit it, would release these springs on the side, and it had the additional advantage of a refill of rubbers with less weight per pound, so that the cost would be less, and it had the further advantage that you could get further adjustment in tightening up on the line after the hole had worn as large as the line.

Mr. Bednar: This catalog, which I believe is in evidence, contains illustrations of these two wire line wipers. Will you explain the steel clad protectors?

A. When I went with the corporation there had been experiments made in stabilizers, which are over-

(Testimony of DeMont G. Miller.)

sized protectors, placed on the drill pipe in the open hole, and the wear was very considerable, on account of rock and gravel; in other words, it wasn't protected like a protector would be, running inside of a pipe. Experience had shown that protectors in the pipe would last for many thousand feet of drilling before they wear out, because they rub against a smooth wall, but in the open hole they would not last very long. So I designed a steel shield that acted the same as the outside casing and also acted as a bearing. [86] Many times the drill pipe hits the side of the hole, the shell stops, and the rubber revolves inside of the casing.

Mr. Bednar: In other words, whenever there is a casing in the well, generally the rubber protectors are used alone, but whenever there is no casing, then the steel clad protector is used; is that correct?

A. That is the location that the steel clad protector is designed for. These are made in several sizes.

Q. By Mr. Lamont: Mr. Miller, you joined the Patterson-Ballagh Company February 15, 1939, did you not? A. Yes, sir.

Q. What had you been doing prior to that time?

A. How long prior ?

Q. Well, let us start immediately prior.

A. I was not working.

Q. For how long a period were you not working?

A. Four of five months.

Q. Prior to that time, that four or five months interval, what work were you doing?

(Testimony of DeMont G. Miller.)

A. Manager of the Sterling Pump Corporation.

Q. Where was that located?

A. Stockton, California.

Q. How long were you employed by them?

A. About two years and a half.

A. In what capacity? A. Manager. [87]

Q. What was your compensation for that work?

Mr. Bednar: Just a minute. At this time I wish to object, on the ground that the question involved here is not what this man was worth to another corporation, but what he was worth to this corporation, and it is incompetent, irrelevant and immaterial.

Mr. Lamont: My answer to that is that precisely that evidence was taken into consideration in the case of Davis vs. Davis Company, a New Jersey case, 52 Atlantic, 715 at page 718, and in a recent work which has just come off the press by George Thomas Washington, entitled, "Competent Executive Compensation." That gentleman is Professor of law at Cornell University Law School, and a member of the New York Bar and the Federal Bar, and that is laid down as one of the——

The Court: I will admit the evidence, subject to the objection, and then I can look into the authorities.

Mr. Lamont: Will you answer, please?

A. $500 a month.

Q. $500 a month? A. Yes.

Q. Prior to that time where had you been working?

A. I think approximately ten years as general manager of the Johnston Pump Company.

(Testimony of DeMont G. Miller.)

Q. In what capacity?

A. General manager. [88]

Q. Where was that located?

A. 2324 East 41st Street, Los Angeles.

Q. What did you receive as compensation there?

Mr. Bednar: The same objection, your Honor.

The Court: The same ruling.

A. My salary varied over that period of time.

Q. Between what limits?

A. As I remember, from $500 to $800 a month.

Q. How did you come to join the Patterson-Ballagh Company?

A. Well, I was taking new work, and I met Mr. Ballagh, and he told me that there might be a chance to buy that concern.

Q. You had known Mr. Ballagh for a great many years, hadn't you? A. Yes, sir.

Q. When did you first meet Mr. Burrell?

A. At the time the option for the sale was drawn up.

Q. As a matter of fact, he put that deal through for you, did he not?

Mr. Bednar: I object to that as calling for a conclusion.

Q. By Mr. Lamont: What part, if any, did he take in connection with the sale of the stock by Patterson to you?

A. He wrote up the option for Patterson and Ballagh.

(Testimony of DeMont G. Miller.)

Q. You had him present, did you not at the meeting [89] before the directors?

A. That is right.

Q. Who outlined the policies of Patterson-Ballagh after you became a part of that company?

A. I did, within my realm as president, and with the approval of the Board.

Q. And who outlined the balance of the policies —Mr. Ballagh?

A. In his department.

Q. From the time you entered the employ of the company up until the time of the beginning of the suit, was the nature of your work which you did for the company changed? A. No, sir.

Q. Prior to these raises in your compensation and that of Mr. Ballagh, I understand the raises took place by a resolution of the Board of Directors on August 22, 1939, March 18, 1940, and November 29, 1940—prior to those raises did you have any conversation with Mr. Dulin? A. No, sir.

Q. I was going to add, as to this particular thing?

A. No, sir.

Q. But you did talk those raises over with Mr. Ballagh? A. Yes, sir.

Q. I am including both in the one question. Did you talk them over with Mr. Burrell? [90]

A. I probably did.

Q. Do you have any definite recollection of it?

A. I have a definite recollection of talking with him, but I don't remember any definite one.

Q. Any what?

(Testimony of DeMont G. Miller.)

A. Any definite one time.

Q. How about Mr. Armington?

A. I don't remember talking with him.

Q. In making these raises, what elements did you consider?

A. The financial state the business was in.

Q. Anything else?

A. The value that the corporation was receiving from the men that were getting the raises.

Q. Anything else?

A. That is all I know about.

Q. Did you consider the fact that you were not paying any dividends, or hadn't paid any dividends since the middle of 1938?

A. Yes, sir.

Q. When you first became connected with this company you apparently looked over the business of the company? A. Yes, sir.

Q. And it was you, was it not, that recommended that the company no longer pay any royalties to Byron Jackson?

A. At what time? [91]

Q. Just prior to the time they stopped paying royalties, which was the middle of 1939?

A. Yes, sir.

Q. June 30th? A. Yes, sir.

Q. Was it on your recommendation that the company ceased paying dividends from then on?

A. Yes, sir.

Q. Did you ever discuss with Mr. Dulan the non-

(Testimony of DeMont G. Miller.)

payment of royalties and the non-payment of dividends? A. Not to my knowledge.

Q. You didn't consult with him as to either action? A. No, sir.

Q. What were your reasons for not paying dividends?

A. At the time the matter came up we were contemplating expansion, and, as the minutes show, we did buy a couple of lots.

Q. You didn't carry that planned expansion far, did you?

A. We didn't carry it through at all. We bought a couple of presses shortly prior to that time.

Q. You gave up the idea; isn't that a fact?

A. Yes, sir.

Q. But you didn't start paying dividends upon giving up the idea of plant expansion?

A. The war was coming on at the same time, and also we [92-93] were contemplating saving the working capital, that it was necessary for this suit that Byron Jackson had with us on royalties, which we did do.

Q. Your earnings were sufficient over and above those reserves, were they not, for the payment of dividends?

A. Yes, sir, but we were on a cash basis. We don't use and credit, and it was necessary to have that much capital, in my opinion, in the corporation.

Q. Did you take into consideration the same elements you mentioned with regard to the non-

(Testimony of DeMont G. Miller.)

payment of dividends in regard to your salary raises?

A. The salary raises were made for a different reason.

Q. Did you consider those elements at all in making those raises? A. Somewhat.

Q. Well, to what extent?

A. The element of the financial condition of the institution.

Q. Is that the only extent to which those matters were taken into consideration? A. Yes, sir.

Q. The minutes apparently show that on March 18, 1940, both your salary and the salary of Mr. Ballagh were raised. That is correct, is it not?

A. Yes, sir.

Q. Did you discuss the raising of those salaries with [94] Mr. Ballagh at the same time, that is, your raise as well as his raise? A. Yes, sir.

Q. And they were presented to the meeting at the same time, were they not? A. Yes, sir.

Mr. Lamont: Take the witness.

Cross Examination

By Mr. Bednar:

Q. Mr. Miller, when you bought the shares from Mr. Patterson did Mr. Burrell represent you?

A. No, sir.

Q. Or did you have another attorney?

A. I had no attorney.

(Testimony of DeMont G. Miller.)

Q. You mentioned plant expansion. What was the nature of that proposed expansion?

A. Prior to this conversation regarding plant expansion, our business was greater than our capacity on the day shift, and we were figuring on enlarging the factory and putting more presses in.

Q. When was the plant expansion dropped, approximately?

A. I can't give you the date. It was after the war started, though.

Q. After the United States was in the war?

A. No; before that. [95]

Mr. Bednar: That is all at this time.

Mr. Lamont: That is all. At this time I have some charts of my own to offer. I would like to offer them in evidence, subject to your right to check them.

Mr. Bednar: They may go in, and I will examine them later.

The Clerk: As a plaintiff's exhibit?

Mr. Lamont: Yes.

The Clerk: Do you want one exhibit number on those?

Mr. Lamont: One exhibit number will be perfectly satisfactory.

The Clerk: They will be Plaintiff's Exhibit 18.

Mr. Lamont: I will get them in order. It will be 18-A——

The Clerk: Instead of 18, it will be 18-A.

Mr. Lamont: B?

The Clerk: 18-B——

Mr. Lamont: 18-C and 18-D?

The Clerk: 18-C and 18-D.

Mr. Lamont: These Exhibits 18A-B-C-D I will hand to the Court.

Mr. Bednar: Have you compared these?

Mr. Lamont: Mr. Chesnut compared them, and if there is any doubt about what they mean Mr. Chesnut will be very glad to explain them to the Court.

Mr. Bednar: I want to check these figures. [96]

Mr. Lamont: That is subject to your right to check. There is one thing I want to make clear, and that is that these exhibits, as far as executive salaries are concerned, only refer to these two gentlemen, the defendants in this action. Mr. Chesnut tells me that the only thing on the statement is the list of royalties, which was checked. May I ask when the Court intends to adjourn, what time?

The Court: Well, now I think will be a good time.

Mr. Lamont: That will be very satisfactory to me. I only have two more witnesses, and the others will be short.

The Court: We will recess until 10:00 o'clock in the morning.

(An adjournment was taken until Friday, July 3, 1942, at 10:00 o'clock a.m.) [97]

Los Angeles, California,
Friday, July 3, 1942.
10:00 A. M.

Mr. Lamont: Mr. Dulin, will you take the stand?

E. S. DULIN,

called as a witness on behalf of plaintiff, being first duly sworn, testified as follows:

The Clerk: Please state your full name.
The Witness: E. S. Dulin.

Direct Examination

By Mr. Lamont:

Q. Mr. Dulin, in what capacity are you connected with Byron Jackson, plaintiff in this case?

A. I am president of Byron Jackson Company.

Q. How long have you been such?

A. Since 1929.

Q. What connection have you had during that period with Patterson-Ballagh?

A. I have been a director since 1930.

Q. And still are? A. And I still am.

Q. In bringing this suit with whom did you discuss where it should be brought, whether in the State Court or the Federal Court?

A. With our attorneys, Chickering & Gregory, [98] particularly yourself, and also with our other attorneys, Lyon & Lyon.

Q. In other words, your conversations, then, were limited to your attorneys?

(Testimony of E. S. Dulin.)

A. And to certain officers and members of the Byron Jackson Company.

Q. The complaint has attached to it three exhibits. You probably recall the demand upon the directors of Patterson-Ballagh, and a letter written by you to Mr. Miller, and a demand upon the other stockholders to take some action in this matter against Messrs. Miller and Ballagh? You recall that, do you? A. I do.

Q. After those different communications were sent to the respective parties, was any action taken by Patterson-Ballagh?

A. Not to my knowledge.

Q. You know of no action having been brought?

A. No.

Q. In 1938 you will recall that the salaries of Messrs. Patterson and Ballagh were raised about, I believe, $1500?

Mr. Bednar: When?

Mr. Lamont: In 1938.

A. Yes. For the exact date and amount I would like to refer to these minutes that are in evidence here. [99]

Q. I now refer you to volume 5 of the minute book of the Patterson-Ballagh Corporation, so that you may refresh your recollection.

A. Yes. That was on October 13, 1938, and the minutes truly reflect what transpired as far as this matter was concerned, in which Mr. Patterson's and Mr. Ballagh's salaries were increased to $1500 per

(Testimony of E. S. Dulin.)

month, at that meeting. It was on a basis of—a month to month basis.

Q. Were you agreeable to that increase, Mr. Dulin? A. I was.

Q. Why?

A. At that time they had been showing certain progress and——

Mr. Bednar: Just a moment. I object to the question as incompetent, irrelevant and immaterial.

The Court: You may answer.

Mr. Lamont: Go ahead. You had better read the witness the part of his answer already given.

(Answer read by the reporter.)

A. And there had been quite a few conflicts between Mr. Patterson and Mr. Ballagh prior to that time, and in looking out for the best interests of the company they had agreed to work on a little more harmonious basis, and, in addition, to set up a procedure that I thought would provide for more efficient operation of the company.

Q. Will you refer to the meeting of March 18, 1940? [100]

A. Yes. I have it now, sir.

Q. At that time it is my understanding that Mr. Miller's salary was increased from $1000 to $1500. That is correct, is it not?

A. Yes. Mr. Miller's salary was increased $500 per month, which made a total of $1500 per month, effective as of March 1, 1940.

Q. Did you acquiesce in that increase?

(Testimony of E. S. Dulin.)

A. I did.

Q. Why?

Mr. Bednar: The same objection.

The Court: You may answer.

A. After the meeting you previously spoke of an analysis was made, and their salaries were subsequently reduced to $1000 a month. No—I am wrong on that, as to the date. I will give my answer, starting again. At the March meeting that we are speaking of, they represented to the Board that it was justified on very fine progress of the company as to sales and earnings, an improvement over what they had been.

Q. What conversation occurred at that meeting?

A. I remember the meeting very well. When I came into the meeting I asked what the purpose of the meeting was, and Mr. Miller advised me that I would shortly find out. After he made a report showing that the volume of sales, etc., was improving, and certain economies in manufacturing had been [101] put into effect, he brought up that the next matter was to be salary. I interjected and asked, salary of himself, and he said yes. I asked him, "And also Mr. Ballagh?" And he said, "Yes." And I said, "Has the matter been determined and discussed?" And he said, "Yes. And the matter, as far as Mr. Ballagh, you will find out about that in due time." I also asked if there had been any consideration as to dividends, and he said that later in the meeting I could bring that up. I might add that, based on the statements made by the op-

(Testimony of E. S. Dulin.)

erating officers of the company, I did not have objection to Mr. Miller's salary being increased, but stated, and the record shows, that it was not to be for any definite period, and with the understanding that it should not remain in effect beyond any reversal in the current trend of favorable business conditions, that should there be an indication ahead that business might take the form of a reversal, it was to be adjusted downward.

Q. Mr. Dulin, did you ever make any objections as to the personnel of the Board?

A. During the time of this——

Q. The time involved in this suit, namely, from the 1st day of January, 1939, to the time of the filing of the action?

A. Yes. The Board has been enlarged prior to that time, and at the time Mr. Miller came in the concern I told him I thought—it had been arranged between Mr. Miller and [102] Mr. Patterson—I didn't know it at that time—for the resignation of certain directors and the substitution of others, and we had, of course, as a director, Mr. Rennie, who, in my opinion, and from work he had done, had a certain amount of ability, and I was disappointed to see that he was slated to be removed, and so stated in the meeting. Since that time, or the time Mr. Miller came in, I have had no opportunity whatsoever of suggesting anybody else for the Board.

Q. You didn't suggest Mr. Armington or Mr. Burrell? A. No, I did not.

(Testimony of E. S. Dulin.)

Q. Did you have anything to do during this period, Mr. Dulin, with the selection of any of the employees?

A. No, not during that period.

Q. Apparently salaries, the record shows, were raised upon three occasions, at the meetings of August 22, 1939, March 18, 1940, and November 29, 1940. Did either Mr. Miller or Mr. Ballagh or anyone else discuss those contemplated raises with you prior to those meetings?

A. No, not at all.

Q. The point has been raised that you voted for the same directors as had been serving before Mr. Miller and Mr. Ballagh. Why did you do that, Mr. Dulin?

Mr. Bednar: I object on the same grounds.

The Court: You may answer.

The Witness: Will you read the question again, please? [103]

(Question read by the reporter.)

A. I had no other choice, being in the minority, and I believe that those directors would, of course, try to serve the best interests of the company, and that it would have done me no good to have objected, being in a minority.

Q. In other words, your objection as to the amount of their compensation——

A. As far as the officers, the record will show that my objections have always been on the amount of compensation, to be an equitable one.

(Testimony of E. S. Dulin.)

Q. At any of these meetings of the Patterson-Ballagh Company which you attended, was anything ever said as to employing either Mr. Ballagh or Mr. Miller as inventors or designers?

A. Never.

Q. Did that subject ever come up in any of those meetings?

A Not in the meetings you are speaking of.

Q. Did that subject come up sometime prior?

A. No, not at a meeting. Only, in these meetings, that they were to carry on the work, when Mr. Miller went in, the same as Mr. Patterson. I knew in the past that Mr. Patterson and Mr. Ballagh had, in my opinion, their line of regular endeavor, were making experiments and improvements, developments, rather, of the products, and had been continuing for years. [104]

Q. The subject was not considered, however, at the time of any of these raises? A. No.

Q. Do you recall who suggested putting Mr. Burrell and Armington on the Board?

A. No, I do not.

Q. But you know that you didn't?

A. I did not.

Q. How big a part in the meetings during this period did Mr. Armington and Mr. Burrell play?

Mr. Bednar: I object to the question as calling for a conclusion of the witness, your Honor.

The Court: He may answer.

A. Taking first Mr. Armington, at any of the meetings that I was present at all, other than to

(Testimony of E. S. Dulin.)

make a motion or to second it, a motion that had been suggested, I don't believe Mr. Armington ever said more than ten words. He did on one occasion answer a question of mine to identify some employee in the Mid-Continent. Mr. Burrell took quite an active interest in taking down notes, writing the minutes, and discussions on tax problems, some on accounting questions, but very little as to the operation of the business.

Q. How about raises in salary?

A. Mr. Burrell never spoke much of those, except to vote on them. I think he voted in the affirmative on all of them. [105]

Q. At the particular time of these raises, Mr. Dulin, what reasons were given you for the raises by either Mr. Miller or Mr. Ballagh?

Mr. Bednar: Was Mr. Dulin at those meetings?

Mr. Lamont: I believe Mr. Dulin was at all of those meetings, on the dates I gave you before, August 22, 1939, March 18, 1940, and November 29, 1940.

The Witness: What was the first one?

Mr. Lamont: August 22, 1939.

A. The first meeting of August 22, 1939, I was not present at.

Q. When did you first learn of that raise, Mr. Dulin?

A. I believe at the next meeting that I attended.

Q. Was any reason given at that time for the raise?

(Testimony of E. S. Dulin.)

A. I would like to go back to the other question —possibly a little before that, through seeing an entry in one of the monthly statements, but I can't recollect which event first happened. What was your next question?

Mr. Lamont: Will you just read my question, please?

(Question read by the reporter.)

A. I was not at the meeting.

Q. I mean at any subsequent conversation.

A. Yes, the great progress of the business, and sales and profits, particularly, and some economies.

Q. Now as to the meetings of March 18, 1940, you were present at that meeting, you said? [106]

A. Yes.

Q. What reason was given at that time?

A. The progress of the company, the profits, which profits later proved to be erroneous.

Q. Did you have any financial statements before you at that meeting?

A. At the meeting of March, 1940, we had a statement of the company, and my recollection is that it was brought up to October 31, 1939, and there were other comments made by both Mr. Ballagh and Mr. Miller, and Mr. Ballagh particularly, as to the current situation.

Q. Did you have any audit before you, an audit by a certified public accountant?

A. Not at that time, to my memory.

Q. How about the meeting of November 29, 1940? Were you present at that meeting, Mr. Dulin?

(Testimony of E. S. Dulin.)

A. The meeting of the 29th of November, 1940, I was not present on that day. The meeting, however, was continued to a later date, when I was present.

Q. Was any reason given you after that meeting as to the increases in compensation prior to that time?

A. Yes. A statement presented by the company, showing their profits of some fifty odd thousand dollars for the eleven months ending October 31, 1940. My memory is that I had this company statement before me later on. The figure of $51,000 was freely used by the officers of the company [107]

Q. Apparently that was not verified by the subsequent audit? A. No, it was not.

Q. I now refer you to Plaintiff's Exhibit 15-D, and ask you whether you are familiar with the document of which that is a copy.

A. Yes, I know of this document.

Q. I believe that there is a provision there, is there not, that upon a sale of stock by Patterson & Ballagh, by Byron Jackson, or Patterson or Ballagh, that such stock first be offered to the other parties to that agreement before being sold to an outsider?

Mr. Bednar: I object to that as not being the best evidence. The document speaks for itself.

Mr. Lamont: I think that is the agreement.

The Court: Is that statement true, Counsel?

Mr. Bednar: I don't know.

(Testimony of E. S. Dulin.)

The Court: Well, you read it, haven't you? It isn't necessary to be so technical.

Mr. Lamont: Here it is: "The parties hereto agree that before any of such parties shall transfer any of the capital stock of said Patterson-Ballagh Corporation to any party or parties other than the parties hereto, such party or parties so desiring to transfer such capital stock, shall offer such capital stock to the other party or parties hereto, upon terms as favorable as such party or parties so desiring to [108] sell such capital stock are able to obtain from any outside party or parties."

Mr. Bednar: I object to this line of questioning, your Honor, on the ground that it is incompetent and immaterial. Mr. Patterson is no party to the suit.

The Court: Well, I don't understand that.

Mr. Bednar: Well, as I understand, the contention is that Patterson, in selling his stock to Mr. Miller, violated this agreement, and Mr. Miller didn't violate and Mr. Ballagh didn't violate it. Whether or not Patterson violated it is not within the issues of this case.

Mr. Lamont: Mr. Ballagh naturally knew about this clause, because he signed the agreement, and apparently he got an old friend of his interested.

The Court: That is what I had in mind. That bare statement by itself, without any other connection, is probably inadmissible, under your objection, but with that suggestion I will overrule the objection.

(Testimony of E. S. Dulin.)

Mr. Bednar: I just want to point out for the record that Ballagh has not violated that agreement.

The Court: No; that is true.

Q. By Mr. Lamont: Mr. Dulin, were either you or Byron Jackson ever offered the Patterson stock before it was sold to Mr. Miller?

A. No.

Mr. Lamont: There is one additional question I want to [109] ask, Mr. Dulin. I think probably in my remarks to the Court I probably overstated my case a little bit.

Q. By Mr. Lamont: What had the relationship been, prior to the time Mr. Miller came into the company, as compared with your relationship with the company after Mr. Miller came in?

A. Going back a good period of years, Mr. Patterson and Mr. Ballagh very often couldn't work very harmoniously together, and I was called on, and it was necessary for quite a while and on numerous occasions, to be a sort of an umpire in their differences, which occasioned a great many meetings with Mr. Ballagh and also with Mr. Patterson, and many of them jointly . The net result of it was that we would be able to get them working harmoniously together for a period of time. And just prior to the sale to Mr. Miller by Mr. Patterson, we had been—and when I say "just prior", I mean three or four months—there had been quite a few conflicts, and we had worked out a plan that we thought and believed would patch up these

(Testimony of E. S. Dulin.)

differences, to the end that the company would be operated more efficiently. This was our program at the time that Mr. Miller came in. In that connection, I believe that I had been the third member of the Board, the rest of the Board Mr. Patterson and Mr. Ballagh, because they stated on a good many occasions that I did enjoy that. One of the things in our arrangement was that we would have quite frequent meetings. After Mr. [110] Miller came in, at the first meeting, which was February 15, 1939, I raised the question as to whether we would continue to have frequent meetings, and Mr. Miller's answer was quite straight-forward, that he had just come into the company, and he would not know until he got better acquainted with it, the necessity of frequent meetings, but, in any event, that that would be determined at a later time. I might add, Mr. Lamont, to your question, that while there were some matters that came up at the time Mr. Patterson and Mr. Ballagh were the controlling stockholders that they wouldn't take up with me prior to a meeting, the large majority of questions, the questions of operations or policy, they would discuss, either together or individually. Now, after Mr. Miller's advent into the company that relationship disappeared.

Mr. Lamont: That is all, Counsel.

Cross Examination

By Mr. Bednar:

Q. Mr. Dulin, you stated, I believe, that you

(Testimony of E. S. Dulin.)

considered the matter of invention, etc., part of the usual duties of Mr. Patterson and Mr. Ballagh for the company?

A. I did in connection with the products of this company.

Q. Can you name any inventions that Mr. Patterson and Mr. Ballagh made prior to January 1, 1939?

A. Not offhand, but I know that they were working on [111] different matters, and that my memory is very vivid on it, due to the fact that in one of these controversies Mr. Ballagh had brought up, and thought it should be a matter with the Board, as to the amount of money and the type of work that Mr. Patterson was doing, for instance, and it was then the policy of the company for a short period of time—it was later not carried through—that they reported at the meetings of the Board about how much had been expended and how much more might be expended on different developments of products. I can also go further, Mr. Counsel, and state——

Q. The only question was, can you name any inventions before January, 1939?

Mr. Lamont: I think the minutes show certain matters in that regard.

Q. By Mr. Bednar: Now, Mr. Dulin, will you turn to page 34 of your deposition, I believe?

Mr. Lamont: Page 34?

Mr. Bednar: Yes.

Mr. Lamont: All right.

(Testimony of E. S. Dulin.)

Q. By Mr. Bednar: I will ask you if your deposition wasn't taken June 23, 1942, and whether or not in that deposition you didn't testify as follows:

"Q—— (By Mr. Bednar): Mr. Dulin, do you know anything about the nature or value of any inventions which Mr. Miller or Mr. Ballagh have made and given to the defendant Patterson-Ballagh Corporation royalty-free? [112]

"A. No."

Did you so testify?

A. Yes, at that time.

Q. Now, Mr. Dulin, referring to your testimony concerning the raises which took place on November 29, 1940—I will find those in the minutes—I believe you were not present at that meeting; is that correct? A. Yes.

Q. And I believe you testified on direct examination that subsequently, as a reason, or one of the reasons for those raises which took place then, a statement of the company was presented showing some $50,000 in net profits for the preceding eleven months period, and that that statement was not verified by a subsequent audit.

A. In the meeting of 1940 the amount may not have been $50,000. I believe there are in evidence here all of the monthly statements of the company, and I would like to have the benefit of turning to those.

Q. Let me indicate to you some portions in the

(Testimony of E. S. Dulin.)

minutes. I believe that statement that was shown at that time indicated some $51,000, did it not?

A. No. It was a later meeting. The minutes refer to a company statement of October 31, 1940.

Q. When that company statement was presented was there any discussion of the fact that it did not reflect any reserves for contingent liabilities arising out of royalties [113] and arising out of taxes?

A. If the statement is in evidence here, could I have it to refresh my memory? I can answer your question, I think, without it, but I would rather have the benefit of it. The statement of October 30th that was at the meeting shows profits for those eleven months of $62,765. Now, what was the other question?

Q. I want to know whether, at the time that statement was presented, it wasn't announced at the meeting that that statement did not reflect contingent liabilities for taxes and royalties.

A. The statement was not given to the meeting, but upon query by me. I asked what was in the fund account, and Mr. Miller stated—which, by the way, was $15,835—that that contained some provisions for contingencies separate. On further questions as to tax matters, tax reserves in there, the rest of it was a contingent liability on litigation and royalties.

Q. I read to you here a portion of the minutes occurring on December 3, 1940, at which the balance sheet indicating the financial condition at October 31, 1940, was presented, and I read this paragraph:

(Testimony of E. S. Dulin.)

"The suggestion was made that a reserve be maintained to cover contingent liabilities of the company, in respect to taxes and possible requirements for the payment of royalties on certain of its products, and it was the consensus [114] of opinion of the directors that this should be done." Did that occur at that meeting?

A. Yes, after the statement I made, and I had been under the impression, particularly in light of Mr. Miller's answer, that there were certain matters there for taxes that the statements would reflect, as the proper reserves, and there had been a resolution or a consensus of opinion of the directors in 1938 to that effect.

Q. Let me ask you this question. Looking at the statement of October 31, 1940, do you find any reserves for contingent liabilities?

A. Contingent liabilities of $4799.25.

Q. Refer to the profit and loss statement. Is there any reserve shown in the profit and loss, that is, that figure that you are contending is incorrect?

A. What is the caption that you want me to find, if I can, on here?

Q. Reserves for contingent liabilities, having to do with income taxes and royalties, possible royalties?

A. There is none there. There are items of taxes in several places.

Q. Those aren't reserves, are they?

A. I am not a bookkeeper or an accountant. But I have read a great many statements. But I think

(Testimony of E. S. Dulin.)

they are set up there as an operating expense, the way they show.

Q. Mr. Dulin, I believe you testified that you had been [115] a director of Patterson-Ballagh Corporation from January 1, 1939, to September 10, 1941? A. Yes; I was a director.

Q. During that period of time approximately how many hours have you personally spent in the offices of Patterson-Ballagh Corporation in connection with attendance at shareholders and directors meetings?

Mr. Lamont: I object to the materiality of that, your Honor.

Mr. Bednar: I want to show how much attention this gentleman has paid to the corporation's business, outside of dividends.

Mr. Lamont: The same objection.

A. I think that can be easily answered by a study of the minutes of the meetings that I was present at. The average length, I would say, was probably a little over an hour. On one occasion I went downstairs through the plant during that period.

Q. Was this the only time that you were in the plant, outside of the shareholders and directors meetings, during that period of time?

A. When I spoke of the plant, I was speaking of the shop downstairs.

Q. Yes.

A. Now, what was your question?

Q. Is that the only time you have been in the

(Testimony of E. S. Dulin.)

plant [116] during this period of time, except for the time that you were at the Board meetings and shareholders meetings?

A. That is right, on their premises.

Q. How long were you down in the plant?

A. About fifteen or twenty minutes.

Q. As I understand your testimony then, you spent about an hour at each shareholders and directors meeting at which you were present, and you spent fifteen minutes in the plant outside of that time?

A. Yes. I don't think there was a meeting that lasted over two hours during the period you are speaking of. I might add to your question that after the position taken by the Patterson-Ballagh Corporation on breaking our royalty agreement, I never felt very welcome around there.

Q. Weren't you invited to go down into the plant at various times to see what was going on?

A. Just on the one occasion, that I recall, during the period you are speaking of. I will add that during this period I was extremely busy on Byron Jackson matters and some very strenuous government matters.

Q. Outside of these visits which you made to the plant of Patterson-Ballagh Corporation, have you had any other sources of information in respect to the nature and extent of the services performed by Mr. Ballagh and Mr. Miller during the period of time in question?

A. No, except as reflected by the monthly state-

(Testimony of E. S. Dulin.)

ments [117] which I would get from time to time.

Q. I understand, then, that at the time that you were objecting to all of these raises in compensation, that you knew nothing of any inventions or devices which had been made and given to the corporation royalty-free by Mr. Ballagh and Mr. Miller?

A. I did not. During the period you are speaking of I was in Washington, at the request of the government, over twenty times, and spent half my time outside of the State of California.

Q. During the period of time in controversy, or at any time since September 10, 1941, have you, as a director, offered any resolution to reduce the compensation paid to Mr. Miller and Mr. Ballagh?

A. I don't think I offered any resolutions. I talked about them plenty. It wouldn't have done me any good.

Q. Have you, at all times during the period in controversy and at all meetings of shareholders at which you were present, voted for the present directors to remain in office?

A. Your question is on shareholders' meetings?

Q. Yes. A. Yes.

Q. And at all meetings of the Board of Directors, during the period of time in controversy, at which you were present, have you not always voted for the election of the same officers, as they are today? [118] A. Yes.

Q. During the period of time in controversy, is it not true that you did not object to any compen-

(Testimony of E. S. Dulin.)

sation until after the repudiation of the license agreement on June 30, 1939?

Mr. Lamont: During the period in question?

Mr. Bednar: During the period in controversy, yes.

Mr. Lamont: That was about a five months period?

Mr. Bednar: Yes.

A. There were no increases that I knew of that were brought to the Board's attention, in salaries, to my memory, from the time that Mr. Miller went in until after Byron Jackson received a notice of the termination or the cancellation or repudiation of that agreement which had been in effect for a good many years. I do not recall any proposal for an increase during that period.

Mr. Bednar: I am looking for one of the exhibits to the deposition. I wonder if we could take a short recess.

The Court: Yes.

(Short recess.)

The Witness: If the Court please, during the recess, it was called to my attention that there was a little confusion in my statement of the raise to Mr. Miller in March of 1940, I believe, in which I was looking at the minutes, and the record probably shows my statement that it was raised from $500 to $1500. I intended and thought I said that it was raised from $1000, by $500, to $1500, so I would [119] like to correct it.

(Testimony of E. S. Dulin.)

Q. Mr. Dulin, I show you a letter dated March 27, 1940, purporting to bear your signature, and addressed to Mr. Burrell. Is that your signature?

A. It is.

Q. Did you cause that to be forwarded to Mr. Burrell? A. I did.

Mr. Bednar: I offer this in evidence.

The Clerk: That will be Defendants' Exhibit I.

Mr. Bednar: I would like to read this letter to the Court, your Honor. This letter is dated March 27, 1940. Your Honor will recall that Mr. Miller was raised from $1000 to $1500, and Mr. Ballagh from $1000 to $2000, on March 18th, about nine days prior to this.

"Referring to your letter of March 23rd, I do not think the draft of the minutes of the directors' meeting properly reflects the essential statements made at the meeting, particularly by myself.

"In connection with the report of the President, it was very definitely set forth that the volume of business that was now being enjoyed was considerably in excess of that experienced during the comparable period of the previous year, etc."

And the sales reports bear that out.

"It was pointed out particularly by the President that the current asset position had materially increased." [120]

And the same is reflected in the reports.

"When it was first mentioned at the meeting that it would be proposed that Mr. Ballagh's salary be increased $1000 a month effective March 1, I very

(Testimony of E. S. Dulin.)

strenuously called to the attention of the directors present that that would result in an executive and administrative salary overhead of the two officers at the rate of $46,000 per year for running a company that from the last preliminary figures available for the 1939 year showed sales of approximately $232,000."

As a matter of fact, the sales for 1939 were about $336,000. Now, continuing: "—which was a marked decrease from the 1938 year, both in sales and profit; and salaries of this amount, based on past performance, were in excess of 12 percent of the total sales and that such compensation was entirely unwarranted and not fair to the minority stockholding. I further stressed the point that salaries should not be increased until dividends could be paid and I thought action on either one was wrong at this time and should await until we were further into the year. However, if this overhead was going to be increased in spite of my objection, that then and then only, dividends should be given consideration. My point was and is that on the present showing"—he is speaking about $232,000—"combined executive salaries of $36,000 a year are all the business can stand and that any increase should not be effective until [121] such time as the company was able to pay dividends.

"The language I used was quite strong and I think yours is very mild and possibly misleading.

"Awaiting your reply, I am

"Yours very truly,

"E. S. DULIN."

(Testimony of E. S. Dulin.)

Q. By Mr. Bednar: Mr. Dulin, in your deposition I asked you whether or not, in using the word "sales" in this last exhibit, where you say sales were approximately $232,000, you were referring to gross or net sales, and at that time I don't believe you recalled. Have you recalled since?

A. No. I always referred to net sales, and I think that is what I referred to here. Now, if I may, I would like to comment on this letter.

The Court: I think you have answered the question.

Mr. Bednar: You have.

Q. By Mr. Bednar: Byron Jackson now owns 250 shares of the defendant corporation, does it not?

A. Yes, sir.

Q. From whom did they purchase these shares?

A. They were purchased prior to my advent into the company, but it is my understanding that they were bought from the Ballagh interests and Patterson interests, in 1928, I believe.

Mr. Bednar: At this time I want to present and offer [122] in evidence some figures prepared for me by the plaintiff, and I will explain them. The evidence indicates that on September 20, 1928, Byron Jackson purchased from Mr. Ballagh and Mr. Patterson 250 shares of Patterson-Ballagh Corporation, at $100 a share, for a total amount of $25,000. The evidence also indicates the amount of dividends that the plaintiff has received on the shares during that period of time. The purpose

(Testimony of E. S. Dulin.)

of this evidence is this: We have here the market value of shares in Byron Jackson on September 20, 1928, which it so happened was approximately $100 a share, the same as the price of Patterson-Ballagh shares at that time. And we have here a list of all the cash and stock dividends paid by the plaintiff on its shares from September 20, 1928. And the purpose is to show what $25,000 invested in the plaintiff on September 20, 1928, would have produced, as compared to what the record shows $25,000 invested in Patterson-Ballagh Corporation on September 29, 1928, has produced. This goes to the sincerity of this plaintiff and the corporate plaintiff. They introduced charts last night correlating the activities of the defendant Patterson-Ballagh Corporation in reference to dividends, gross sales and salaries, and if they are serious in criticising the proportion of salaries to dividends, then we ought to be entitled to show what their practice has been.

Mr. Lamont: I object to its materiality, if the Court please. [123]

Mr. Bednar: The purpose is to show the sincerity of this plaintiff.

Mr. Lamont: What another company may have done in regard to the payment of dividends or salaries or anything else certainly wouldn't be competent evidence as to the value of the services rendered by Mr. Miller and Mr. Ballagh, and certainly wouldn't be competent.

Mr. Bednar: This exhibit shows the correlation

(Testimony of E. S. Dulin.)

between the salaries and the dividends paid by Patterson-Ballagh Corporation, and the inference is that there were a lot of salaries and no dividends. Now I want to show what the practice of Byron Jackson was, to show their good faith.

Mr. Lamont: They were employed by Patterson-Ballagh, and not by Byron Jackson.

Mr. Bednar: They are criticising us, and I want to show the good faith of their contention.

Mr. Lamont: It is certainly a collateral issue.

Mr. Bednar: Let me make an offer of proof.

The Court: All right.

Mr. Bednar: At this time I offer to prove by this witness that Byron Jackson Company purchased 250 shares of Patterson-Ballagh Corporation on September 20, 1928, for $25,000; that from September 20, 1928, to the end of 1941 the plaintiff received at least $121,275 in cash dividends on its 250 shares of defendant Patterson-Ballagh Corporation; and that the highest market value of plaintiff's shares of [124] stock on or about September 20, 1928, was approximately $100 per share; that the same amount of money, towit, $25,000, invested by plaintiff in shares of the defendant corporation on September 20, 1928, would have purchased the same number of shares, to-wit, 250, in Byron Jackson Company on September 20, 1928; that the sum total of all cash and stock dividends declared and paid by the plaintiff on said 250 shares from September 20, 1928, to the end of 1941, did not exceed approximately $6700; that for the period from Sep-

(Testimony of E. S. Dulin.)

tember 20, 1928, to the end of 1941, $25,000 invested in Patterson-Ballagh Corporation has produced at least $121,275 in dividends, whereas $25,000 invested in plaintiff would have produced only about $6700 in cash and stock dividends. In addition, I offer to show that the compensation of Mr. Dulin, for example, for 1941, was $50,000. I am just comparing their dividend and salary policy with the policy on our part that they criticise.

The Court: Well, that would be interesting, of course, but it probably wouldn't have any probative value. You could probably find a thousand corporations in Southern California that that would apply to.

Mr. Bednar: The thing I am trying to get at here——

The Court: I understand what you are trying to get at. I don't think it is proper.

Q. By Mr. Bednar: Going back again to the amount of time you spent in the Patterson-Ballagh Corporation plant, [125] would you say the total amount of time you spent during 1939, 1940 and 1941 exceeded ten hours?

A. Let me see the minute book and count the meetings, and that might help me a little. Your question is directed, Counsel, I think, to the time spent on the premises of Patterson-Ballagh?

Q. That is right.

A. And it refers to 1939, 1940 and 1941?

Mr. Bednar: Up to September 10th. Maybe we can let Mr. Dulin finish this computation.

(Testimony of E. S. Dulin.)

The Witness: I am still in 1939.

Mr. Bednar: I think we had better let you finish your computation, and ask you about it later. That is all for the present, until he does that.

Redirect Examination

By Mr. Lamont:

Q. This is the letter written by Mr. Dulin to Mr. Howard Burrell, dated March 27, 1940, marked Defendants' Exhibit I. I again show you this letter, Mr. Dulin, and ask you whether you have any comment to make in regard to that figure of $232,000. A. I have.

Q. What is it?

A. This letter written by me is a little ambiguous on the face of it. The figure of $232,000 refers to the sale [126] of protectors and stabilizers, and at the time that that figure was determined it was from direct inquiry by me to Mr. Ballagh, and he produced some figures out of a drawer on the left-hand side of his desk. My question was, what were our sales for the year 1939, on the bread and butter part of the business of Patterson-Ballagh, which had always been, namely, protectors and stabilizers, and he gave me a figure of $232,000, and when I figured on the back of a piece of scrap paper there about the percentage to total sales, the $46,000, it obviously shows here that I was figuring on a larger amount, which was in excess of $232,000, and my question to Mr. Ballagh was, was that a decrease in sales of protectors and stabilizers over the pre-

(Testimony of E. S. Dulin.)

vious year, and he said it was. You have introduced in evidence a chart showing for the year 1939 your sales of protectors and stabilizers, of $233,000, and apparently I made an error of $1000.

Q. Mr. Dulin, I now show you what purports to be your copy of the assets and liabilities of Patterson-Ballagh Corporation as of October 31, 1940, accompanying the report, apparently, and I believe that some of the notes on that are in your handwriting, are they not?

A. Yes; these are my handwriting. This was my copy of the statement I had at the meeting, in which the figures of October 31, 1940, were reviewed.

Q. Does that refresh your recollection as to any element [127] there?

A. Yes. Just as I testified, when I asked Mr. Miller what was in this $15,835 item marked "Fund account," he stated, "Reserve for taxes and reserve for contingencies." I thought at the time that he answered the question.

Q. Counsel for the defendant has gone into the matter of the time you devoted to Patterson-Ballagh, especially the amount of time you were on the premises of Patterson-Ballagh during the period from January 1, 1939, to September 10, 1941. Did your time stop there, or did you devote other time as well to Patterson-Ballagh?

A. Yes, other time studying statements, talking with our auditors, discussions with the different members of our organization in the oil fields as to

(Testimony of E. S. Dulin.)

certain things they were doing, the developments in the oil fields, foreign questions, and all.

Q. That was a substantial amount of time, was it? A. Yes, quite a bit of time.

Q. There was one point that slipped by me yesterday in having counsel put in these charts. I am now referring to Defendants' Exhibit F. Apparently on that exhibit there is a statement to the effect that the investment of Byron Jackson Company in Patterson-Ballagh is $25,000. I will show you the exhibit, Mr. Dulin. Does that figure properly reflect the investment of Byron Jackson in the corporation of Patterson-Ballagh? [128]

A. It does not. When I joined the Byron Jackson Company, their books reflected, and still reflect, an investment in Patterson-Ballagh Corporation of $100,000, $25,000 in cash and——

Mr. Bednar: Just a minute. I believe all this is hearsay. You didn't come to the Byron Jackson Company until after the deal, did you?

A. That is correct.

Mr. Bednar: I don't think this is admissible, then.

Mr. Lamont: If the Court please, it refers to how the matter is carried on the records of our company.

Mr. Bednar: Were those records ever communicated to us?

Mr. Lamont: I don't know whether they were or not.

(Testimony of E. S. Dulin.)

Mr. Bednar: I believe the evidence is purely hearsay, your Honor.

The Court: It probably is, It would be hearsay.

Mr. Lamont: All right. Take the witness.

Mr. Bednar: That is all.

Mr. Lamont: That is all, Mr. Dulin, I guess.

The Witness: Shall I finish this one here?

The Court: You can take your book down and work on it.

Mr. Bednar: I want to ask Mr. Dulin one more question.

Recross Examination

By Mr. Bednar:

Q. Referring again to your letter of March 27, 1940,—— [129] A. Yes.

Q. At the time you wrote that letter, did you know anything about any items sold by the corporation other than protectors and stibilizers?

A. Yes; I knew they had certain lines, and that they had had for a good many years.

Q. Did you know what the gross profit was on the sales of these other non-protector items?

A. I did not. I tried to find out on a good many occasions, and could not.

Mr. Bednar: That is all.

Mr. Lamont: That is all. The next witness I am going to produce is an expert witness, and I am going to tell the Court in advance that he is quite deaf, and it may be a little difficult to examine him. Call Mr. Bunch. [130]

E. S. BUNCH,

called as a witness in behalf of plaintiff, being first duly sworn, testified as follows:

The Clerk: State your full name, please.

The Witness: E. S. Bunch.

Direct Examination

By Mr. Lamont:

Q. Mr. Bunch, where do you reside?

A. Los Angeles.

Q. How long have you resided here?

A. Nine years, the last time.

Q. What occupations have you pursued, say in the last nine or ten years?

A. I was an analyst and statistician, with experience as a stock broker and investment counsel and financial writer and public relation counsel.

Q. During that period have you had occasion to go into the amount of executive salaries of numerous companies? A. Repeatedly, yes.

Q. Why did you happen to go into these matters?

A. Mostly research work, compiling data for use in the valuation of corporate securities.

Q. Not merely, then, for the purposes of this case? A. No.

Q. Let me ask you this question, Mr. Bunch. Let us [131] assume a small manufacturing business, in other words, what might be called a specialty business.

Mr. Bednar: Just a minute. I will abide by whatever your Honor wants me to do, but I would

(Testimony of E. S. Bunch.)

like to ask this gentleman a few questions on voir dire before they get to the point of asking for a conclusion.

Mr. Lamont: That is perfectly satisfactory to me.

The Witness: I am quite deaf.

Q. By Mr. Bednar: Mr. Bunch, I take it that you intend to testify concerning salaries in other corporations, do you? A. If asked, yes.

Q. What types of corporations are those?

A. General.

Q. General? A. Yes.

Q. Are any of these corporations engaged in the oil tool business? A. Yes.

Q. Are any of them engaged in the business of manufacturing and selling rubber for industrial purposes?

A. In some of them there would be, yes; I mean they would carry rubber articles among their lines.

Q. In the oil tool business?

A. In the oil tool business.

Q. Rubber articles? A. Yes. [132]

Q. Are the salaries that you are going to testify to salaries of presidents and chief executives?

A. Heads, chief executives, yes.

Q. Do you know whether or not those executives ever invented devices and gave them to their corporations royalty-free?

A. I don't think I do, no.

Q. Do you know what the duties of these vari-

(Testimony of E. S. Bunch.)

ous officers concerning whom you are going to testify were?

Mr. Lamont: I might simplify this a little. I am not going to ask this witness anything about the value of an inventor's services. I am going to approach that through a different means.

Q. By Mr. Bednar: Do you know anything at all about the defendant Patterson-Ballagh Corporation?

A. No, except its financial data and the salaries that the officers draw and the general facts of its financial setup and operation.

Q. Do you know anything about the business of making and selling rubber specialties in the oil tool business?

A. I am engaged in the rubber business. I own a part of one, but not in the oil tool business.

Q. Do you know anything about these items here? Have you ever seen them before?

A. I know generally the usage of them, yes. I am in the oil business more or less myself. [133]

Q. Have you seen these in operation?

A. Yes, I have seen them.

Q. Do you know anything about hydraulic applicators?

A. No, not especially, because I have never been connected with the operating end. I have been on the derrick and seen the things, probably, and paid no attention.

Q. Do you know anyting about the importance of the hydraulic applicator in the drilling of wells?

(Testimony of E. S. Bunch.)

A. No, not specifically.

Q. Do you know anything about the importance of these protectors in the drilling of wells?

A. No, I know their usefulness.

Q. Do you know anything about pipe wipers?

A. I have seen them, and seen them used, and that is all.

Q. Do you know anything about the importance of using them. A. No.

Q. Are you in business for yourself?

A. Yes.

Q. When did you first meet Mr. Dulin?

A. Last Monday.

Q. Did you ever know him before then?

A. No.

Q. Have you ever prepared statistical studies of Byron Jackson? [134]

A. No. I have casually studied them with relation to securities.

Q. But concerning the corporate salaries to which you will testify if allowed to, you don't know whether or not the persons who received those salaries ever gave any inventions to their corporations royalty-free?

A. In some specific case I probably would. My studies cover a great number of corporations. Offhand, though, I couldn't reply that I do. I know I have studied Ford and Spicer Motors, and those various companies, and in many cases there have been inventions by the chief executives among

(Testimony of E. S. Bunch.)

them. But to call it out of thin air, I couldn't do it, no.

Q. Do you know anything about the duties of Mr. Ballagh or Mr. Miller in this case?

A. I have read the depositions, and that is pretty well covered.

Mr. Bednar: I guess that is all. It goes to the competency of this witness. I don't believe his testimony is going to cover any services in addition to duties in the way of inventing. Otherwise his testimony will have to bear out whether he knows anything about rubber specialties in the oil tool business. There is a great difference between those and metal parts. So I will object to the testimony.

Mr. Lamont: I submit the objection.

The Court: Go ahead. [135]

Q. By Mr. Lamont: Mr. Bunch, let us assume a small manufacturing company or business, in fact a specialty business, which has only two executives, and which has an invested capital and surplus of between $200,000 and $250,000, which has net sales ranging from $300,000 to $400,000 per year, and which has earnings ranging from $20,000 to $30,000 per year before taxes, and let us assume that these two executives devote their entire time and attention to the carrying on of that business, laying aside all questions as to their possible value as inventors or designers, what would you say, from your investigation of questions of executive salaries, would be the reasonable value of their services to the company?

(Testimony of E. S. Bunch.)

A. I would say approximately $10,000 each.

Mr. Bendar: May I have the last question and answer?

(Record read by the reported.)

Mr. Lamont: Mr. Bunch has compiled some very interesting figures. It may be objectionable for me to put that in evidence, but for the sake of the record I will——

Mr. Bednar: Can we look it over and then we will see? I will look it over during the noon hour.

Mr. Lamont: Certainly. Outside of offering this testimony, that is all I have with this witness.

Mr. Bednar: I understand that this witness does not base his estimates upon inventors' services of any kind?

Mr. Lamont: No. I didn't ask him to go into that, [136] because I don't think he is competent to testify along those lines. I don't think his testimony on those lines would aid the Court. I am going to approach that through another witness, as I stated before.

Cross Examination

By Mr. Bednar:

Q. Mr. Bunch, Do you know anything about the importance of patents and inventive rights in the oil tool business, and more particularly the use of rubber industrially in the oil tool business?

A. I know generally about the very high value of many of those patents, yes.

Q. Do you know of companies that have enjoyed

(Testimony of E. S. Bunch.)

very prosperous years, and then a new patent has issued and has practically run them out of business?

A. Not exactly that, but I have known of companies that have enjoyed very prosperous years, and then, due to some betterment of the article of their competitors, have proceeded to lose money, of course.

Q. And lose their business to the competitors?

A. Yes.

Q. Then, in your estimation, the patent rights of a company which is engaged in manufacturing and selling rubber specialties in the oil tool industry are very important?

A. I would consider them so, yes. [137]

Mr. Bednar: That is all.

Mr. Lamont: That is all. That is all for the time being. Do you want to look over that?

Mr. Bednar: Yes.

Mr. Lamont: Mr. Chesnut, will you take the stand? [138]

JOHN D. CHESNUT,

called as a witness in behalf of the plaintiff, being first duly sworn, testified as follows:

The Clerk: Will you please state your full name?

The Witness: John D. Chesnut.

(Testimony of John D. Chesnut.)

Direct Examination

By Mr. Lamont:

Q. Mr. Chesnut, where do you reside?

A. In La Canada, California.

Q. What company are you connected with?

A. Byron Jackson Company.

Q. How long have you been connected with that company?

A. Approximately 12 years.

Q. In what capacity?

A. Manager of the patent and new development department.

Q. Will you be a little more specific as to what that covers.

A. I have charge of the investigation of new products that are brought to the company from the outside, and new products developed from within the company, from the standpoint of their patentability, whether or not they might infringe any other patent, whether or not they are suitable for manufacture by our company, and investigation into the manufacturing cost and probable selling price and market conditions and profits to be made. I also supervise the [139] work of others who are engaged in the detail of that work in the patent end and in the development of it.

Q. In the course of your work with Byron Jackson, do you have occasion to become acquainted with what is normally paid to an inventor or designer for full time service by a corporation?

(Testimony of John D. Chesnut.)

Mr. Bednar: I object to that. I think the question is too general. If you want to direct it to some specific company——

Mr. Lamont: I will bring out what Byron Jackson paid, if you want it.

Mr. Bednar: No. It is a relative matter. Steinmetz is paid tremendous sums.

Mr. Lamont: It seems to me that is more a question of cross-examination, Counsel. I will submit the objection.

Mr. Bednar: I don't know how it would aid the Court, but I will object.

Mr. Lamont: I will be very frank with regard to this expert testimony. I put it in for one reason. I think, from the facts before the Court, the Court is perfectly safe to figure out the compensation. There is one California case which is rather annoying, which seems to infer that if you prove all the facts and circumstances and don't prove the extent of such expenses, the Court should find that the case hadn't been established, and that is the real reason for offering it. I will take the ruling of the Court. [140]

The Court: I assume there would be so much variation between what experts would be paid that I don't see that it would be of any particular interest.

Mr. Lamont: That is all, then. That is all, that is, in chief. Mr. Dullin has gotten this other matter figured out. Do you want to put him back on?

The Court: All right. [141]

E. S. DULIN, recalled

Cross Examination

The Witness: A. About 18 hours.

The Court: What is the question?

Mr. Bednar: The question was, how much time did he spend on the premises of Patterson-Ballagh Corporation during 1939, 1940, and up to September 10, 1941.

The Court: And the answer is 18 hours?

A. Around 18 hours at all the meeting that were called, that I appeared at.

Mr. Bednar: That is all.

Mr. Lamont: That is all. [142]

DEFENDANTS' CASE

Mr. Bednar: First of all, the inference has been left here that this other suit for the repudiation of royalties doesn't amount to much.

The Court: Well, it doesn't, as far as I am concerned. It might as far as the parties are concerned. I am interested in only one thing here, whether these salaries are proper.

Mr. Bednar: I appreciate the Court's viewpoint. The only ting is, the influence has been left that there was a conspiracy here to repudiate, and to raise salaries, and to stop dividends. As a part of showing that conspiracy, the inference has been left—well, maybe this royalty proof doesn't amount to anything—in order to refute that inference, I

have the brief here, which I would like to introduce.

The Court: I think Judge Hollzer will have to read the brief in that case.

Mr. Bednar: The briefs are rather lengthy. Call Mr. Burrell.

HOWARD BURRELL,

called as a witness on behalf of defendants, being first duly sworn, testified as follows:

The Clerk: State your name, please. [143]

A. Howard Burrell.

Direct Examination

By Mr. Bednar:

Q. Mr. Burrell, are you an attorney?

A. I am.

Q. Approximately how long have you been practicing in California? A. Since 1926.

Q. Will you state briefly when you met Mr. Miller for the first time, the defendant?

A. I met Mr. Miller in the early part of the year 1939, the latter part of January or the early part of February.

Q. And when did you first meet Mr. Ballagh?

A. I met him in the fall of the year 1934.

Q. Will you state briefly your connection with the Patterson-Ballagh Corporation prior to the time you became a director?

A. In the fall of the year 1934 they were involved in certain patent litigation involving title

(Testimony of Howard Burrell.)

to a patent to a manual applicator or protector, and my firm was associated with Lyon & Lyon as counsel in the defense of that action. The action was commenced, as I recall, about December, 1934, and was tried in the Superior Court of this County, and appealed to the Supreme Court, and finally concluded in the year 1937 or the early part of 1938. In the year 1938 I [144] handled one matter for the corporation, that of the amendment of its by-laws, to increase the number of directors from three to five. It is possible the corporation consulted me on other matters. I have one in mind, and that was the matter of this judgment in this other litigation with Mr. Bettis, which was handled while this litigation involving the manual applicator was pending. During the early part of 1939, at the end of January or the first part of February, Mr. Ballagh and Mr. Patterson came to my office and said they had a transaction they wanted reduced to writing with Mr. Miller, covering an option from Mr. Patterson to sell to Mr. Miller his shares of capital stock of Patterson-Ballagh Corporation. I represented Mr. Patterson in that transaction. It was comparatively simple. It was the preparation of a letter and note on the option agreement.

Q. When did you become a director of Patterson-Ballagh Corporation?

A. I became a director of the Patterson-Ballagh Corporation during the month of June, 1939.

Q. When did you first become general counsel for the Patterson-Ballagh Corporation?

(Testimony of Howard Burrell.)

A. A few months after that. I wouldn't want to say definitely—around the fall of 1939. I am general counsel, if that is what you mean.

Q. Yes.

A. I had been special counsel in these litigation matters [145] I mentioned before, and had handled a couple of special matters for them. Lyon & Lyon were their general counsel.

Q. From January 1, 1939, to September 10, 1941, do the minutes of all the meetings at which you were present correctly reflect what took place at those meetings?

A. They do, to the best of my ability, for the reason that I drew them from notes taken at the meetings at which I was in attendance.

Q. What salaries were Miller and Ballagh receiving when you went on the Board?

A. $1000 a month each.

Q. Were you present at the meeting on August 22, 1939, at which time Mr. Ballagh received a raise? A. I was not.

Q. Do you know whether you were present at a subsequent meeting and approved the minutes of August 22, 1939? A. I was.

Q. What were your reasons for approving the $4000 raise given to Mr. Ballagh?

A. Well, there were several.

Mr. Lamont: I think that is incompetent, irrelevant and immaterial, if the Court please. We have here merely the question of whether his compensation was reasonable.

(Testimony of Howard Burrell.)

Mr. Bednar: Do I understand that the only question in this case is whether or not the compensation is excessive, that there is no contention of lack of good faith, or anything [146] like that?

Mr. Lamont: Oh, certainly—that contention also. Perhaps it might be material to that issue. I will withdraw the objection.

A. Mr. Ballagh during this period had devoted a great amount of time to his efforts as sales manager of the company. He had had a great part in litigation pending in Oklahoma, or commencing in Oklahoma, involving applicator patents, and he had completed the perfection of the hydraulic applicator, which I considered the most important thing that had as yet been received by the company in the last few years.

Mr. Lamont: Is counsel putting him on as an expert on patent matters or not?

Mr. Bednar: I am asking for his reasons for——

Mr. Lamont: I ask the Court to strike out the last remark as to the value of the patented devices.

The Witness: It was not a patented device.

Mr. Lamont: Well, the value of the invention, the so called invention.

The Witness: As yet.

The Court: Go ahead.

A. The company, after the flush period of its existence, and during its flush period, had used what is known as a manual applicator, which was covered by patent issued to the company as the

(Testimony of Howard Burrell.)

assignee of Bettis, which was the subject of this litigation I previously referred to, but [147] which had many difficulties in the field of operation, which were answered by the hydraulic applicator, which enabled the company to hold its protector customers to it.

Mr. Lamont: It seems to me this is subject to the same objection. We have a lawyer on the witness stand. You are not a patent attorney, are you, Mr. Burrell? A. That is correct.

Q. By Mr. Bednar: In this litigation from 1934 to approximately 1938 that you said you were engaged in, did that case involve applicators of all kinds?

A. Yes, it did, from the very first to the last applicator that had been in existence.

Q. How many applicators, do you recall, were involved?

A. Six or seven, all of which were models of manual applicators, from the very first one that had been developed, involving various improvements, as distinguished from the hydraulic applicator. It was a manual applicator, and not a hydraulic applicator.

Mr. Bednar: I might say that I offer this testimony to show the reasons which this witness had in mind, and not for the purpose of actually showing the value of the hydraulic applicator itself. In other words, the question is the good faith.

The Court: These other gentlemen connected

(Testimony of Howard Burrell.)

with the corporation would know more about it than the attorney.

Q. By Mr. Bednar: Did you have any other reasons for [148] approving the initial raise of Mr. Ballagh's salary?

A. None other than I stated, other than that, as I say, he was engaged in a great many activities outside the ordinary course of his duties, in developing articles and devices. Up to that time, during my connection with the company, he hadn't done anything in this field of any consequence, and during the year 1938 and 1939 he devoted himself, in addition to his duties as sales manager, to the development of additional articles for manufacture and distribution.

Q. Were you present at the meeting on March 18, 1940, at which Mr. Miller's compensation was raised from $1000 a month to $1500 a month?

A. I was.

Q. What were your reasons for approving Mr. Miller's raise?

A. Mr. Miller had come in—he had been in the company about a year. He had taken charge of its finances and the operation of its factory and the purchasing of its supplies. He had shown an improvement in financial condition through his efforts by the ratio of current assets to liabilities, which was improving at that time, and had improved some before. I had been informed of various efficiencies he had installed in the plant and in the office. I had discussed with him various

(Testimony of Howard Burrell.)

activities that he was engaged in, in the development of new devices for sale and distribution. Mr. Dulin was at the meeting and said he had no objection to [149] the compensation of $18,000 a year, or $1500 a month, and in view of the matters I have in mind, and in view of the fact that Mr. Dulin had no objection, I approved it.

Q. What were your reasons for approving Mr. Ballagh's raise in compensation from $1000 to $2000 a month, at the meeting of March 18, 1940?

A. The company, when this protector, which was the Bettis Protector, was acquired by it, paid over $400,000 in royalties to Mr. Bettis for this protector, until the patent on it was declared void, and many thousands of dollars to Byron Jackson under the license agreement.

Mr. Lamont: What is the materiality of this?

The Witness: I am stating my reasons. And Mr. Ballagh, during the fall of 1939 and 1940, the early part of 1940, had developed—a few days prior to that time had filed an application for letters patent on the lip protector, which I felt was of great value to the company. I felt and I still feel that it was——

Mr. Lamont: That is subject to the same objection I have continually urged. The witness is an attorney, and should follow the rules as far as testimony is concerned.

The Witness: I was answering the question, Mr. Lamont.

The Court: After all, he is stating the reasons,

(Testimony of Howard Burrell.)

and while they may not be valid, they are his reasons.

A. I considered the lip protector a great improvement over the old type of what was known as the Bettis Protector. [150] And Mr. Ballagh was still working on other devices, these activities being carried on outside of his ordinary and usual duties as sales manager and secretary and treasurer of the company, and I thought the value to the company of his services and the fact that he had indicated an intention to transfer to the company without other consideration, without any requirement of royalties, patents on the various devices that he was working on and had developed, justified the increase in salary.

Q. Were those approximately the same reasons for the voting of additional compensation in November, 1940?

A. With the additional reason that, commencing with the proceedings involving the hydraulic applicator, an interference trial was conducted in Oklahoma, and as a result I had negotiated, through the efforts of Mr. Ballagh, what I considered a most favorable cross licensing agreement with the interferring party Barnes, which I felt was worth many thousands of dollars to the company.

The Court: We will suspend here until 2:00 o'clock.

(An adjournment was taken until 2:00 o'clock p. m. of the same day.) [151]

Afternoon Session — 2:00 o'Clock P. M.

Mr. Lamont: Counsel, how about this list that I gave you when Mr. Bunch was on the stand?

Mr. Bednar: I forgot to look it over, but you can put it in evidence.

Mr. Lamont: All right. I will put it in evidence now. I have a carbon here, which, if satisfactory to the Court, I will offer the carbon to be marked as plaintiff's exhibit, the oppropriate number.

The Clerk: That will be Plaintiff's Exhibit No. 19.

PLAINTIFF'S EXHIBIT No. 19

COMPANIES WHOSE TWO HIGHEST SALARIED EXECUTIVES RECEIVE LESS THAN $50,000 PER ANNUM

Compiled from the roster of corporations listed on the Los Angeles Stock Exhange.

The Exchange roster was chosen as a desirable source of data for the following reasons:

(a) The list is representative of numerous types of California industry, particularly of the oil business. In character, the companies range from long-established, nationally known institutions to comparatively small enterprises.

(b) As measured in importance by capital invested and scope of operations, indicative of the responsibility carried by the executives, the list reflects a comprehensive graduation of business size, from very small to quite large undertakings.

(c) The Exchange constitutes a satisfactory cross-section of industrial organizations in California from which may be ascertained data on actual practice of corporations in fixing maximum remuneration of their executives.

(d) Lastly, because of Government requirements of companies listed on national security exchanges, sworn statements revealing such salaries are available in each instance in the records of the Securities and Exchange Commission on file at the Los Angeles Stock Exchange.

The statistics herewith in all cases were taken from the Securities and Exchange Commission records.

EXECUTIVE SALARIES, CORPORATIONS

Fiscal Year	Corporation	Two Highest Salaries	Capital and Surplus	Profit or Loss	Dividends Paid
12/31/41	Gladding McBean & Co.	$49,673	$7,447,062	$ 603,984	$159,908
12/31/40	Western Pipe & Steel Co. of Calif.	45,200	4,576,212	312,477	156,645
6/30/40	Hancock Oil Co. of Calif.	44,150	4,613,811	1,138,528	784,000
8/31/41	Consolidate Steel Corp.	44,000	4,841,381	667,518	373,246
12/31/40	Sontag Chain Stores Co.	40,120	2,128,971	225,931	141,889
12/31/40	Lane Wells Co.	38,500	2,206,900	605,977	522,000
12/31/40	Emsco Derrick & Equipment Co.	38,400	3,687,015	82,475*	.....
12/31/40	Ryan Aeronautical Co.	37,688	1,424,821	358,344	.....
12/29/40	Van de Kamp's Holland Dutch Bakers	37,100	1,204,215	203,209	113,581
12/31/40	Los Angeles Investment Co.	32,950	6,262,240	161,474	.....
12/31/40	Puget Sound Pulp & Timber Co.	31,600	5,034,611	795,553	855,786
12/31/40	Blue Diamond Corp.	30,060	2,201,131	55,936	145,863
12/31/40	Electrical Products Corp.	28,578	2,120,478	342,674	262,022
12/31/40	Universal Consolidated Oil Co.	24,530	1,612,734	228,190	99,977
12/31/40	General Metals Corp.	21,200	1,216,189	259,623	32,230
12/31/40	Pacific Clay Products Co.	21,037	1,454,661	53,236	.....
12/31/40	Taylor Milling Co.	21,000	2,421,223	197,589	100,000
12/31/40	Bolsa Chica Oil Corp.	15,675	1,034,417	47,907*	.....
12/31/40	Weber Showcase & Fixture Co.	14,822	2,060,724	58,692	17,494

* Figures in Red.

Executive Salaries Corporation—(Continued)

Fiscal Year	Corporation	Two Highest Salaries	Capital and Surplus	Profit or Loss	Dividends Paid
5/27/40	Solar Aircraft Co.	14,034	747,819	51,546	11,500
6/30/40	Menasco Manufacturing Co.	14,000	873,021	190,137*	.....
6/30/40	Roberts Public Markets, Inc.	$13,000	$ 631,205	$206,252	$43,905
12/31/40	Bandini Petroleum Co.	10,680	1,538,075	2,412	99,375
12/31/40	Holly Development Co.	9,650	721,569	51,691	36,000
12/31/40	Merchants Petroleum Co.	9,400	167,904	2,082*	.....
10/31/40	Intercoast Petroleum Co.	8,600	428,668	3,080	.....
12/31/40	Lincoln Petroleum Co.	8,020	143,369	27,613*	.....
12/31/40	Oceanic Oil Co.	6,650	256,502	6,555*	59,722
12/31/40	Nordon Corp., Ltd.	5,935	377,153	10,793	.....
12/31/40	Mascot Oil Co.	5,400	329,492	4,789	25,000
12/31/40	Rice Ranch Oil Co.	5,013	284,502	12,089	20,000
12/31/40	Occidental Petroleum Co.	4,895	140,785	418*	.....
12/31/40	Holly Oil Co.	4,800	399,505	10,092*	.....
2/28/41	Mount Diablo Oil, Mining & Development Co.	3,950	139,201	13,874	23,374
12/30/41	Patterson-Ballagh Corp.	53,666	201,023	22,999	.....

[Endorsed]: Filed July 3, 1942.

Mr. Lamont: I might add that the witness is still in Court, so if there is anything the Court doesn't understand we can put him back on.

Mr. Bednar: Who prepared this?

Mr. Lamont: Mr. Bunch prepared it.

Mr. Bednar: Mr. Burrell.

HOWARD BURRELL,

recalled.

Direct Examination,

resumed.

By Mr. Bednar:

Q. Mr. Burrell, I believe this morning you testified to your reasons for approving additional compensation for Mr. Miller and Mr. Ballagh, or for Mr. Ballagh, rather. You mentioned various inventions and other devices. Do you recall [52] the other devices?

A. There were other devices he was working on at the time, one of which he referred to, a pipe wiper, for example. The sales of that have doubled each year since it was offered on the market. At that time there hadn't been a patent on this device, and the patent was issued in February, 1942, and it was under application at the time. And then he developed other items of lesser importance. I attributed greater importance to the hydraulic applicator and the protector.

Q. During the years 1939, 1940, and up to September 10, 1941, have you had any disagreement

(Testimony of Howard Burrell.)

with Mr. Ballagh and Mr. Miller concerning the affairs of this corporation?

A. You mean Board meetings?

Q. Yes.

A. Well, there have been several things that I haven't seen eye to eye with them on. They brought up at one time the question of taking cash that represented reserves for taxes or royalties and investing them in interest-bearing securities, and Mr. Dulin and I both opposed that, and their proposal was abandoned. They carried an item of good will on the balance sheet in the amount of some $80,000, that I thought should have been charged to the earnings surplus account, and a rather small item of a similar nature—I forget the name of it—an installment equipment item of about $1100. Mr. Dulin and I suggested that those be [153] written off, and finally we were able to succeed in that. And we never approved very much of the accounting methods that were being pursued by the company. They did not set up on their operating statements accruals for taxes or for royalty items. So the month to month operating statements did not correctly reflect or furnish a complete picture of the company's program. At the end of each year we would receive an auditor's statement, which showed the earnings in a different amount, as a result of the deductions of these reserves, that I felt should have been included in the monthly statements. In February of this year, at the organization meeting of the Board of Directors, Mr. Dulin and I made the sug-

(Testimony of Howard Burrell.)

gestion, and it was ordered that these changes be made in the accounting practice. I wouldn't say that these were controversies with Mr. Ballagh or Mr. Miller, but they were at least disagreements with their methods of procedure.

Q. How much time have you devoted to the affairs of the Patterson-Ballagh Corporation in the year 1939, for example, approximately?

A. I would say in 1939 I devoted at least 75 to 100 hours.

Q. And in 1940, or can you tell me that?

A. In 1940, probably the same amount.

Q. And in 1941?

A. Considerably more in 1941, due to certain litigation.

Q. At every meeting at which you were present in 1939, [154] 1940 and 1941, did you, after the meetings, go through the factory and see the new devices that had been discussed?

A. I don't believe—I wouldn't say I did that at every meeting. I customarily did it. On a few occasions I did not do so.

Q. Do you recall any occasions when Mr. Dulin was invited to go down and make an inspection of the factory, and he did not do so?

A. I took a trip through the factory one time with Mr. Dulin, and there were other occasions when we could have gone through, should we desire, but we didn't do so. I do know he went through once when I was along.

Q. Did Mr. Dulin frequently announce at the

(Testimony of Howard Burrell.)

various meetings when he arrived that he would like to get the meeting over so that he could go early?

A. Mr. Dulin was busy with other matters; he was president of Byron Jackson Company and other matters, and he was involved, so that he couldn't spend too much time at the meetings.

Q. Have you ever acted as personal attorney for Mr. Ballagh or Mr. Miller?

A. I never acted as personal attorney for Mr. Miller. Mr. Ballagh, or Mrs. Ballagh, had a small collection made a year ago, approximately, I believe, that they handled through a young man in my office, which was done with very little effort and didn't amount to a great deal. [155]

Q. When you received from Mr. Miller and Mr. Ballagh the various demands that are set forth at the end of the complaint as exhibits, what action did you take?

A. I got in touch with Mr. Miller and ascertained from him that Mr. Ballagh was in the Mid-Continent, and in view of the fact that Mr. Ballagh was away I wrote to Mr. Dulin a letter, advising him that as soon as all the interested parties could be assembled I would attempt to arrange a meeting at which his suggestions would be considered.

Mr. Lamont: I won't make any point about this not being an original.

Mr. Bednar: I wonder if I could read this into the record. It is the only copy we have.

Mr. Lamont: Suppose you read it into the record?

(Testimony of Howard Burrell.)

The Witness: May I see the letter?

Q. By Mr. Bednar: Is this the letter that you referred to? A. Yes. [156]

Mr. Bednar: The letter reads as follows:

"August 15, 1941

"Byron Jackson Co.,
P. O. Box 1307,
Arcade Station,
Los Angeles, California.

Attention Messrs. E. S. Dulin, W. M. Beadle and W. H. Weise.
Re Patterson Ballagh Corporation

Gentlemen:

"We wish to advise that there has been handed to this firm for attention your recent communications addressed to Patterson-Ballagh Corporation and to its officers, directors and shareholders in respect to the matter of the institution of proceedings against DeMont G. Miller and J. C. Ballagh for the purpose of recovering from them certain alleged excess compensation mentioned in said communications.

"It is desired to report that the matter of calling and holding a meeting of the board of directors of Patterson-Ballagh Corporation for the purpose of considering and acting upon the requests and demands contained in your communications is under consideration, and that it is expected such a meeting will be called as soon as arrangements can be made to assure that all interested persons will be in attendance.

(Testimony of Howard Burrell.)

"This firm has no authority to express an opinion as to the correctness of the statements and allegations contained in your communications, and this letter is written solely for the purpose of advising you of the matters hereinbefore [157] mentioned.

"Very truly yours
MUSICK & BURRELL
By HOWARD BURRELL."

Q. By Mr. Bednar: Mr. Burrell, did you receive from Mr. Dulin this letter of March 27, 1940, which is in evidence here?

A. I have it here. It hasn't got an identification number here.

Mr. Lamont: That is a photostat. The original is in evidence.

Mr. Bednar: It is in evidence here as Defendants' Exhibit I.

The Witness: I did.

Q. Do you know what the sales were in 1939?

A. The statements of the company give them as $336,000.

Q. Do you know where Mr. Dulin obtained the figure of $232,000? A. I do not.

Q. Do you remember any episode at the meeting where Mr. Dulin asked about the sales of protectors, and Mr. Ballagh opened a drawer and drew out some papers and gave a figure of $232,000?

A. No; I wouldn't recall that.

(Testimony of Howard Burrell.)

Q. I show you from the minutes a letter included in the [158] minute book, following the meetiing of June 27, 1939, such letter being dated June 23, 1939, addressed to Patterson-Ballagh Corporation, attention of Mr. D. G. Miller, and composed of two pages, and signed by yourself. You sent that letter to Mr. Miller? A. I did.

Q. Are you of the same opinion today as you were in that letter?

A. Subject to correction by Judge Hollzer, I am.

Mr. Bednar: That is all.

Cross-Examination

Q. By Mr. Lamont: Mr. Burrell, I understood you to testify that you handled the sale of the Patterson stock to Mr. Miller. Is that correct?

A. I did.

Q. I now refer you to Plaintiff's Exhibit 15-D, and ask you whether at that time you were familiar with that agreement? A. I was not.

Q. What was the first time you saw that agreement?

A. Two or three weeks prior to the time of the preparation and sending of that letter which Mr. Bednar just mentioned, in June, 1939, at which time I procured all of the files of Patterson-Ballagh Corporation with regard to this controversy involving the repudiation of the license agreement. [159]

Q. Who gave them to you?

A. As I recall, Mr. Ballagh brought them in to me.

(Testimony of Howard Burrell.)

Q. Did you discuss this agreement prior to that time with either Mr. Ballagh or Mr. Miller?

A. No, I did not.

Q. Who employed you in regard to putting the stock sale through.

A. Mr. Miller and Mr. Patterson and Mr. Ballagh appeared at my office one morning and said that negotiations were being conducted with Mr. Miller to buy Mr. Patterson's stock, and asked if I would prepare the note and option agreement.

Q. Who paid your bill?

A. Mr. Patterson.

Q. When did you become general attorney for the Patterson-Ballagh Company?

A. After June, 1939, several months, a retainer arrangement was agreed upon.

Q. But you did certain work for them prior to that time, did you not?

A. Yes, in association with Lyon & Lyon, excepting for the one matter of amending the by-laws.

Q. Lyon & Lyon were never their general attorneys, were they?

A. I don't know as they ever had any general counsel other than Lyon & Lyon. I think Mr. Caughey, of Lyon & Lyon, [160] advised them in patent matters.

Q. They are patent lawyers, aren't they?

A. That is correct. But I know Mr. Caughey handled their matters for them. I know Mr. Caughey handled several suits for them.

(Testimony of Howard Burrell.)

Q. Anything else?

A. I know Mr. Caughey and Mr. Ballagh were very close socially, and I know they discussed the business of the company, and I assume Mr. Caughey would do what civil work they had done.

Q. You don't know that they were ever paid a general retainer, do you?

A. I do not know.

Q. I believe you testified, with regard to the meeting of March 18, 1940, I believe it was, at which Mr. Ballagh's salary and Mr. Miller's salary was increased, that you voted in favor of the increase of Mr. Miller's salary because Mr. Dulin had no objection?

A. I said that was one of the factors taken into consideration.

Q. Did you take that into consideration in regard to raising Mr. Ballagh's salary?

A. I did.

Q. What other elements did you take into consideration as far as Mr. Miller was concerned?

A. The fact that he had taken over the production [161] phases of the business of the company, had, I understood, installed certain efficiencies, both in the plant and in the office, had made or was contemplating at the time, certain plant improvements, some of which were consummated and some of which were not, was working on devices for the company that they would receive royalty free, and there had been an improvement in the ratio of current assets to current liabilities, a slight improve-

(Testimony of Howard Burrell.)

ment, by the end of 1939. The ratio was approximately 5 to 1 at the end of 1938, and approximately 10 to 1, I believe, at the end of 1941. And that progress was going forward during this period.

Q. Of course you didn't take into consideration the progress in 1941 in fixing salaries in 1940, did you?

A. No, but that scale of improvement was going on; it was in progress; it was about half way through.

Q. When it came to an actual vote at those meetings, you never have voted against either Miller or Ballagh, have you?

A. There have only been two meetings at which I was—I wasn't present at the meeting of August, 1939.

Q. I asked you, at the meetings which you attended, did you ever vote against either of them?

A. I have not.

Q. If I get your testimony correctly, Mr. Burrell, you figured—if I am not correct in this regard, correct me—you figured that the increases were warranted on account of [162] the inventions made by Mr. Ballagh; is that correct?

A. Not alone. That was one of the factors.

Q. Was that one of the principal factors, in your mind?

A. It was a substantial factor.

Q. Who owned the inventions at the time?

A. They had either been transferred or were being transferred, or he had indicated that he would

(Testimony of Howard Burrell.)

transfer them to the corporation. I don't know which inventions you are talking about.

Q. I am talking about the ones that Mr. Ballagh claims he invented, and the ones you took into consideration in regard to this salary raise.

A. For example,the pipe wiper——

Q. When these inventions were originally made, whom did they belong to? A. Ballagh.

Q. And is it your position that until they were transferred to the company they still belonged to Ballagh?

A. Yes. Mr. Patterson, for example, had made a patent some four or five years previously, which he took in his own name and refused to recognize the company as having any interest in it of any character.

Q. I take it, then, that some of these increases were in lieu of royalties; is that true?

A. Yes—it was distinctly to the advantage of the company to compensate Mr. Ballagh and Mr. Miller on a salary [163] basis which was flexible, rather than on a royalty basis, which would exist for the life of the patent, binding the company, as it had been bound before by the license agreement I testified about earlier.

Q. The ordinary royalty agreement would have been flexible, would it not, to the extent that it would have gone up and down with the number of sales of the device?

A. It would be flexible from the standpoint of sales, but not the amount. The company was forced

(Testimony of Howard Burrell.)

out of the export business practically by the Byron Jackson Company on that contract, because it wasn't flexible.

Q. You have stated that that was one of several facors? A. I said a substantial factor.

Q. How would you have figured the royalties had you taken the other course and provided for royalties? How would you have figured the values of these patents?

A. The best illustration of that can be shown by the cross license agreement with Barnes and the company, covering the hydraulic applicator, where a royalty of 25% for each protector put on a drill pipe is paid.

Q. What do you take into consideration in figuring what a royalty should be?

A. The monopoly created by the device.

Q. What else?

A. The commercial value of the device.

Q. How do you determine that? [164]

A. By its success in the field into which it is offered.

Q. What else do you consider?

A. The gross profit that is obtainable from the manufacture of the device.

Q. Anything else?

A. The extent of the field in which the device may be usable.

Q. What else?

(Testimony of Howard Burrell.)

A. And the benefit conferred upon the purchaser of the device.

Q. Now let us take the pipe wipers, Mr. Burrell. How much did you take that into consideration in fixing these raises?

A. That was taken into consideration. As I said before, the lip protector and the hydraulic applicator were more important, in my mind.

Q. What were the gross profits that were being derived from the pipe wipers?

A. About 80%. They were selling at five times cost.

Q. 80% of what?

A. The item sold around $30, and, as I recall, it cost around $5.

Q. Did you figure at all the net profit?

A. In a general way. I know the net profit on the non-protector items. As to the net profits on the protector items, I know that from talks with Mr. Ballagh, in connection [165] with the business affairs of the company.

Q. You don't mean the actual amount?

A. I don't mean from the standpoint of cost accounting. I mean from general discussions with the officers of the company.

Q. You don't mean actual or total?

A. No; I mean percentage.

Q. How about the line guide?

A. The line guide was not invented by Mr. Ballagh. They were paying royalty on that to another inventor. You mean the wire line wiper?

(Testimony of Howard Burrell.)

Q. How about the tubing protector?

A. The tubing protector I know very little about. It is nothing but a small drill pipe, with small protectors, or tubing, that is all.

Q. Did you know what the profits were from that item?

A. I couldn't tell you that. The item only sells, as I understand, in small volume. There is a new type tubing protector which has just been completed, I believe, by Mr. Miller.

Q. Have you any knowledge of the net profits derived from any of the articles sold by this corporation?

A. It would be impossible to ascertain that without cost accounting.

Q. You didn't know that at the time when you voted these raises? [166]

A. No. I knew there was a larger gross profit——

Q. And you don't know it now?

A. I know there is more net profit, yes. What I mean is, I couldn't segregate the net profit on every item made by the company during the year ending November 30, 1941, without cost accounting.

Q. And the same would apply to 1940 and 1939?

A. Each year, yes.

Q. Then you never suggested, as counsel for the company, an additional operating agreement with these gentlemen having to do with compensation for inventions?

A. I thought it was particularly adverse to the

(Testimony of Howard Burrell.)

interests of the company to allow these gentlemen to take patents out and have them enter into royalty agreements with the company on them, so I have not recommended them.

Q. I believe you mentioned this lip protector as being an important element. Did the adding of the lip add anything to the size of the business in regard to protectors?

A. Not for the protector business, but it replaced the old protector entirely, it having many advantages over the old protector. It gives control of the protector market. This company now sells 75% of the protectors sold over the world.

Q. But it didn't increase the protector business materially?

A. No, because the protector business throughout the [167] world was not increased.

Q. Mr. Burrell, from your knowledge of the company, what would the monthly purchases amount to, on an average?

A. I would say approximately 20% more or less of the sales; possibly 15%.

Q. You are talking about gross sales?

A. Yes. There is a small differential between net and gross sales in this company anyway.

Q. Yes, I understand. You commented also, I believe, in regard to raising Mr. Miller's salary, that there had been some increase in efficiencies. Can you be more specific in that regard?

A. There were a number of employees in the office, and the number of employees was reduced, and

(Testimony of Howard Burrell.)

the same work was accomplished by those remaining. In the plant two new presses were installed and the plant equipment was rehabilitated and the plant renovated, and it was obvious from those activities that the efficiency of the shop had been improved.

Q. Those would have been increases in efficiency that should have been accomplished by any executive officer, irrespective of raises in salary; isn't that true?

A. I believe that is true. He accomplished them, though, and they hadn't been accomplished before by his predecessor.

Q. What personal investigation did you make of these matters? [168]

A. I practically lived with the applicator for four years.

Q. During what time?

A. From 1934 to 1938.

A. How about the others?

A. That was the manual applicator. Then the last two years of that period I was working on the hydraulic applicator. They are two different types of devices.

Q. What investigation did you make of the tubing protector?

A. I said I knew very little about it.

Q. How about the pipe wipers?

A. The pipe wiper—I talked with Mr. Ballagh, the sales manager of the company, on a number of occasions, and I found that sales had doubled each year that had been on the market. From my investi-

(Testimony of Howard Burrell.)

gations. I understand they carry about 80% gross profit, and are becoming a more and more acceptable item.

Q. You mentioned patents. Have you received any patents?

A. I have not reecived a patent. I understand the application is pending. That is all I know about it.

Q. You don't know as yet whether that is a patentable device?

A. I know it is not patented. The application is pending. [169]

Q. I said "patenable."

A. No, I wouldn't know.

Q. At the time you were discussing these raises did you call anyone else's attention to the value of the inventions?

A. At what time, do you mean?

Q. March or November—any of the three times involved in this case.

A. At practically every meeting Mr. Ballagh had there lists of these devices, prices for them, and on occasions we would ask him what percentage of his sales were non-protector and what were protector sales, and I assume from the figures he gave and the fact that these manuals were there and in everybody's possession, if they cared to look at them, that we all knew about these various devices.

Q. You didn't call Mr. Dulin's attention at the time of these salary raises to the value of the inventions, did you?

(Testimony of Howard Burrell.)

A. In the meeting of December 3rd, at the meeting which was adjourned—If I may see the minute book—it was a meeting adjourned from November to the early part of December, because of Mr. Dulin's absence, at the very first part of the meeting, and on account of his ability to return on the adjournment date. The meeting was originally commenced on November 29, 1940, and adjourned to December 3rd, so that Mr. Dulin could be in attendance. At the adjourned portion of the meeting Mr. Dulin asked Mr. Ballagh at considerable [170] length about what these other items were doing and how they were selling, and there was some discussion in that field, and I didn't think, at the conclusion of that, that it was necessary for me to point out to Mr. Dulin what the items were, because I thought he understood what they were.

Q. What was the date of that meeting?

A. That was December 3, 1940.

Q. That was after——

A. That was after the March meeting, but it was the one at which this bonus for the year 1940 was approved.

Q. The bonuses had been already fixed by the meeting of November 29th?

A. But which were being discussed in the meeting of December 3rd. The meeting was still in session.

Q. But the bonuses had already been passed?

A. Yes, sir.

Q. Let me get at it this way. But the actual resolution for the bonuses occurred November 29th?

(Testimony of Howard Burrell.)

A. That is correct. We were re-discussing it.

Q. In these meetings apparently you referred to discussions as to protectors and non-protectors. Did you discuss articles other than protectors as a class or group, or discuss them independently?

A. I don't know what you mean.

Q. I mean there were several items going to make up the gross sales of the company. One item is the protectors? [171]

A. Yes, sir.

Q. And there are a number of other items. There are pipe wipers, and tubing protectors, line guides, and in discussing these items other than protectors proper, did you discuss them as a group or did you discuss them separately item by item?

A. At times we discussed them as a group, and at times we would discuss them separately. I remember one meeting where Mr. Ballagh gave an extended report on the litigation that had been concluded successfully in Oklahoma, involving the hydraulic applicator and the cross license agreement with Mr. Barnes. I remember discussion of the wire line guide, which was a patented product on which we were paying a royalty, and discussion of various items. I don't mean to intimate that at each meeting we went into a discussion of each item of the company.

Q. You testified as to the number of hours you devoted to the service of the company. Did that figure apply to hours just spent on the premises, or did it apply in your office?

(Testimony of Howard Burrell.)

A. It applies to both on the premises and in my office, and conferences with Mr. Ballagh both at the office of Lyon & Lyon and in my office.

Mr. Lamont: Take the witness.

Mr. Bednar: No further.

Mr. Lamont: You won't want Mr. Bunch any further, will [172] you?

Mr. Bednar: No.

The Witness: Mr. Lamont, can I be relieved at a quarter past three? I have to be at a meeting at four. That will give you a half hour to decide?

Mr. Bednar: Call Mr. Morris. [173]

RAY WALDEN MORRIS,

called as a witness in behalf of defendants, being first duly sworn, testified as follows:

The Clerk: State your full name, please.

A. Ray Walden Morris.

Direct Examination

Q. By Mr. Bednar: How long have you worked for Patterson-Ballagh Corporation, Mr. Morris?

A. It will be 8 years in November.

Q. Have you worked as a salesman all the time in the field?

A. No, I was in the plant up until the 1st of April, 1937.

Q. And what territory were you located in after that date?

(Testimony of Ray Walden Morris.)

A. I was sent to Corpus Christi, Texas.

Q. How long did you remain down in Texas?

A. 10 months.

Q. From there where did you go?

A. To Shreveport, Louisiana.

Q. How long did you remain there?

A. 18 months.

Q. When you left Shreveport, where did you go?

A. I was transferred back to Los Angeles.

Q. And you have been here ever since? [174]

A. Yes, sir.

Q. Can you describe generally your duties as salesman?

Mr. Lamont: How would that be material?

Mr. Bednar: The only thing I want to show is the fact that he not only sells, but he takes the devices out in the field and puts them on, and watches them in operation.

A. We sell them and install them and keep checks on them to see how they work, and their life, and all of that, everything pertaining to that.

Q. When did you first hear of the hydraulic applicator transfers?

A. It was in 1939.

Mr. Bednar: I want to introduce these pictures showing the applicator with the transfer, just to give the court an idea of what I am talking about.

Mr. Lamont: If I understand, this is not a device sold by Patterson-Ballagh?

(Testimony of Ray Walden Morris.)

Mr. Bednar: No. But the evidence will show that without this device we would not be in business, as far as protectors are concerned. It is the means of applying a protector upon a drill pipe.

Mr. Lamont: You were in business, were you not, long before that device was invented?

Mr. Bednar: That is right. But somebody else came along with a better mousetrap, and we had to do something to save ourselves. I would like to introduce this one, for the time [175] being, as Defendants' exhibit next in order.

The Clerk: Defendants' Exhibit J.

Q. By Mr. Bednar: Now, I wish you would explain very briefly how this applicator works.

A. Take a protector and set onto this cone here, and the cone is put over this shelf here in the center, and the protector sits on this expander, and this sleeve is taken and placed on the cone, and this pushes the protector on up; this raises up and is pushed on up onto the sleeve, and the cone drops down inside, and the protector transfers on the cone, on up on this sleeve, and the sleeve has a locked place, and it fits on this, and has a lock on it so that the sleeve is held stationary while the protector is being pushed up on it. And the sleeve is slid any place on the particular joint of pipe, and is pushed off with the set screw. We have a flange here that works on here, that this set screw pushes against. That pushes against the protector with the sleeve, and pushes it on up. Here is a picture.

(Testimony of Ray Walden Morris.)

Q. The picture appears on page 1934 of the catalog that is in evidence.

A. It shows the entire operation. The machine here, it shows it placed into position, as I explained, and this shows the operation under way, the expander going up and pushing the protector up onto the sleeve. This shows the completed job here. Here it has been put over the drill pipe and has been pushed off here. That is the complete [176] operation right there.

Q. Mr. Morris, when did you first hear of the hydraulic expander with the transfer sleeve?

A. It was in the summer of 1939.

Q. And where were you at that time?

A. I was in Shreveport, Louisiana.

Q. Was there another similar device in use in that area at that time?

A. There was an applicator in use down there that installed protectors hydraulically, but did not have a transfer sleeve like ours, but it did install the protectors hydraulically.

Q. Can you tell the advantage of the transfer sleeve?

A. The main advantage of the transfer sleeve is that you can install the protector any place on the customer's drill pipe that he might want it.

Q. You don't have to stop drilling operations?

A. No; you install it on the rig, and can install it any place.

(Testimony of Ray Walden Morris.)

Q. Can you install the protectors away from the well?

A. Yes, and relieve them of any hazard of the old applicator, and at the same time leave them free to go in while it is going on.

Q. When you first obtained this hydraulic applicator that you have described, with the transfer sleeve, were there any customers that you obtained thereafter who had not been [177] buying from you, but were buying from competitors?

A. Yes, there was, in that particular territory.

Q. Can you name some of them?

A. Well, there would be F. H. Brown Drilling Company; the Standard Oil Company; Newark Oil Company, they called it; the Big West Drilling Company; the Delta Drilling Company; and the Penrod Drilling Company. Those are a few of the companies.

Q. Have the competitors that existed at that time since ceased using the hydraulic applicator?

A. As I understand, they have an injunction against them.

Q. Is there a similar applicator or comparable device in use in California?

A. Yes, there is.

Q. How does it differ from this device, if any?

A. It differs in that they place the protector on an expander that pushes in the protector on the sleeve, and it is removed from the sleeve on the drill pipe by hydraulic pressure.

Q. After the protector is placed on the sleeve

(Testimony of Ray Walden Morris.)

and carried over and put on the drill pipe, after the sleeve is put on the drill pipe, then in transferring the protector from the sleeve onto the drill pipe, this other device was a hydraulic method?

A. That is correct. [178]

Q. Whereas you use a mechanical method?

A. That is correct.

Q. Which is the faster?

A. From our experience, our method is the faster.

Q. Without this hydraulic applicator, can you estimate what the effect would have been upon your own personal sales of protectors?

Mr. Lamont: Just read that question.

(Question read by the reporter.)

Mr. Lamont: I object to the question as calling for a conclusion of the witness.

The Court: He may answer.

A. In my own personal sales, 90%.

Q. By Mr. Bednar: Your own personal sales would have been 90% less? A. Yes.

Q. What does the other 10% represent?

A. The other 10% would represent small operators, and it wouldn't make any difference particularly what method was used to install the protectors, and competitors' business.

Q. When did you first hear of the lip protector, Defendants' Exhibit D for identification?

A. That was in 1939.

Q. And where were you at that time?

(Testimony of Ray Walden Morris.)

A. I was in Los Angeles at that time. The particular place was in Arkansas, part of my territory. [179]

Q. Were you present at the first job when the lip protector was put on?

A. Yes; I installed the first one.

Q. What had happened just prior to that time?

A. A protector without lip had ruined the man's drill pipe and caused him to have three different twist-offs in three different days, and we either had to put lips or something to stop the grooving, or we wouldn't have a customer, as far as he was concerned.

Q. This was the first time a lip protector was used? A. Yes, sir.

Q. Has that customer ever complained since then?

A. He is still buying the protectors.

Q. Has he had any grooving of his pipe since then, to your knowledge?

A. To my knowledge, he hasn't.

Q. Have you ever had a customer who has used the lip protector, and, after having used it, ordered protectors without it?

A. I have not, no, sir.

Q. Are you acquainted with Mr. Miller's wire line wiper?

A. Yes. We started to experiment on those in 1939.

Q. Are there any competing devices?

(Testimony of Ray Walden Morris.)

A. There is one competing device that I know of.

Q. In your territory how many of the wire line wipers in use do you estimate are sold by Patterson-Ballagh Corpora- [180] tion?

A. I would say 90%.

Q. You are acquainted with Mr. Ballagh's drill pipe wiper? A. Yes, sir.

Q. Are there any competitors?

A. Yes, sir; there is one competitor.

Q. In your territory, how many of the drill pipe wipers in use do you estimate are sold by Patterson-Ballagh Corporation?

A. In my territory, about 98%.

Q. When did you first hear of Mr. Miller's steel clad protector?

A. My first experience with it was in 1941.

Q. Is this the device you are referring to?

A. Yes, sir, that is it. I had heard of a trial and usage prior to that.

Q. Do you know of any competing devices?

A. Yes, sir; there is one competing device. It isn't in existence at present; it isn't being manufactured.

Q. From your experience in your territory, what has been the reaction of the customers who have used this device?

Mr. Lamont: I object to the question as incompetent, irrelevant and immaterial, and asking for the opinion and conclusion of the witness. How

(Testimony of Ray Walden Morris.)

does he know what reaction there has been? [181]

Mr. Bednar: Well, from what they tell him.

Q. By Mr. Bednar: Who, to your knowledge, uses these steel clad protectors?

A. Barnsdall.

Q. Where? A. At Cascade.

Q. What have they told you about the steel clad protector?

Mr. Lamont: I object to that as incompetent, irrelevant and immaterial.

The Court: Well, just one person——

Mr. Bednar: This is a new device, your Honor, and of course it may be one field, but it goes to show the prospects for the device. For instance, I expect to show by this witness that in this particular field they can't use any other protector except this one.

The Court: Well, he may answer.

A. Mr. Frehoda, drilling superintendent there, told me that they had more than paid for themselves in saving and tool joints, and the ones he had used on that, they dulled 168 bits, in an average of eight hours drilling time to each bit, and it had proven more than its worth to him, to the company, and Barnsdall wanted them in that particular field.

Q. By Mr. Bednar: What is there about that field which makes the use of this protector vital?

A. Well, the formation is very abrasive. There is a [182] very abrasive formation there, and if there is nothing on there to protect the tubes it

(Testimony of Ray Walden Morris.)

wears them down and they have to be rebuilt, built up or thrown away.

Mr. Bednar: You may take the witness.

Cross-Examination

By Mr. Lamont:

Q. Mr. Morris, how long did you say you have been employed by Patterson-Ballagh?

A. Since November, 1934.

Q. Were you employed during the period from January 1, 1939, until September 10, 1941?

A. Yes, sir.

Q. What was your salary or compensation?

A. My salary?

Q. Yes. A. $200 a month.

Q. All during that period?

A. From 1939?

Q. January 1, 1939, to September 10, 1941.

A. I was getting $180 a month.

Q. You mentioned a figure of 90% in regard to hydraulic applicators—I think it is 90%.

A. Yes, sir.

Q. What was your reason for saying 90%?

A. Due to the fact that our competitor had a hydraulic applicator—— [183]

Q. Do you base that conclusion upon any other circumstance?

A. We were referring to the hydraulic machine.

Q. I know what you were referring to, but did any other circumstance enter into your ultimate conclusion of 90%?

(Testimony of Ray Walden Morris.)

A. Well, not in that personal thing.

Q. You didn't have any fact or figures to support——

A. From my personal experience in the field.

Q. General observation?

A. From my own particular experience, and from what I was told by others.

Q. Anything else? A. No, sir.

Q. How many competitors were there as to hydraulic applicators? A. Two.

Q. Who were they?

A. That is the Bettis Rubber Company, and E. M. Smith, you are talking about.

Q. In this particular territory, now, you are talking of? A. Yes, sir.

Q. As a matter of fact, there were other hydraulic applicators, were there not?

A. Only one that I had any interference with.

Q. You are limiting all this to your territory?

A. Yes, the territory I have been in. [184]

Q. Was there another one?

A. I don't remember the name of the company. They were selling protectors in Louisiana.

Q. You knew Mr. Patterson, did you not, of Patterson-Ballagh? A. Yes, sir.

Q. As a matter of fact, he had a hydraulic applicator, did he not, a patent on one, and at one time refused to turn it over to Patterson-Ballagh?

A. That must have been when I was gone.

Q. You don't know one way or the other?

A. No, sir.

(Testimony of Ray Walden Morris.)

Q. How did you arrive at your 90% in regard to wire line wipers?

A. By my observations in the field and my selling in the field.

Q. Do you know what the gross sales by Patterson-Ballagh of wire line wipers amounted to in 1941? A. No, sir; I haven't any idea.

Q. This chart apparently shows $2,050.60 and total gross sales of over $336,000.

A. They are a small priced article.

Q. You referred to drill pipe wipers, and you are still consistent, with 90%. Upon what do you base your 90% conclusion?

A. On my sales in the field and my observations around [185] the rigs.

Q. You had no facts and figures?

A. Only what I have been told by different operators.

Q. In other words, you arrived at your conclusion in the same way with regard to that item as you did with regard to the other items, did you not? A. Yes, sir.

Q. How many other territories are there where wire line wipers and drill pipe wipers are sold, besides the territory you know about?

A. As far as my knowledge is concerned, they are sold almost universally wherever they are drilling.

Q. But you have no knowledge of the other territories, though? A. No.

(Testimony of Ray Walden Morris.)

Q. How much do steel pipe protectors sell for per protector, steel clad protectors?

A. It depends on whether it is a 5-inch drill pipe or a 4½-inch drill pipe or a 3½.

Q. Give us the figures for some of those.

A. The ones that Barnsdall ran, $36 apiece.

Q. There are not many of them sold, are there?

A. They probably bought 150.

Q. Apparently the gross sales of the company in 1941 amounted to only $597.29. Do you know whether any were sold in 1940? [186]

A. No, sir, I do not.

Q. Apparently this chart doesn't show any sales in 1940.

Mr. Bednar: It was a new device.

The Witness: It was being worked up.

Q. And not at all, apparently, in 1939. You say you have been with the company quite a while?

A. Yes, sir.

Q. As a matter of fact, before this lip protector came into being you sold, over a great period of years, the other protector, did you not?

A. You mean the company or myself?

Q. The company. A. Yes, sir.

Q. And you personally, did you not?

A. From 1937.

Q. Any competitive items as to drill pipe wipers?

A. Is there?

Q. Yes, are there?

A. There is one company.

(Testimony of Ray Walden Morris.)

Q. One company, that is all? A. Yes, sir.

Q. And you are talking about your territory?

A. Yes, sir.

Q. How about the steel clad protector?

A. There is, or there was one competitor. I understand [187] they are not making them now.

Mr. Lamont: That is all.

Mr. Bednar: Mr. Ballagh.

The Court: We will have our afternoon recess now.

(Short recess.)

Mr. Bednar: Mr. Ballagh. [188]

J. C. BALLAGH,

a witness heretofore duly sworn, upon being recalled on behalf of defendants, testified as follows:

Direct Examination

By Mr. Bednar:

Q. Mr. Ballagh, from January 1, 1939, until September 10, 1941, have you ever voted at any meeting in favor of your own salary?

A. No, sir.

Q. During that period of time were notices of all the meetings sent to Mr. Dulin? A. Yes, sir.

Q. Directing your attention to the non-protector items that your company sold during that period of time, was the margin of profit on non-protector items substantially more than on protectors? A. Yes, sir.

(Testimony of J. C. Ballagh.)

Q. Will you give us a little bit of your background?

A. I graduated from the Colorado School of Mines in 1910 as a mining engineer and as a metallurgical engineer, and after graduation I went to Mexico and worked in a mining camp for a year, and returned to California and worked in the oil fields for something over a year at Maricopa, California. From there I returned to Mexico for a few months, and from there I went to Texas, and I remained in Texas for about 11 years, during which time I was in the machinery [189] business and in the oil tool business, and also in connection with the drilling of oil wells. And from there I went to Arkansas and drilled a number of wells. And from there I went to Oklahoma, and then I returned to California and went into the turbine pump business as an installer for Lane-Bowler Company. From that company I went to the Kimball Pump Company, for whom I worked about two years. And then I went to the Pomona Pump Company, for whom I worked about a little over a year. And from there I went to the Johnston Pump Company, and worked for that company a little over a year.

Q. When did you first meet Mr. Miller?

A. I think I met him at college, but I can't remember meeting him at school very much. The first time since that time was when I returned to California after being down in the Midcontinent. He

(Testimony of J. C. Ballagh.)

was then manager of the Lane-Bowler Pump Company, and he gave me a job installing pumps, where I worked for about three months. And then later on, after I worked for the Pomona Pump Company for a year, I went to work for him as a salesman, and worked for him for approximately a year.

Q. When did you first encounter the use of rubber industrially?

A. When I was working for the Pomona Pump Company, I found that that company was making quite a success in the sale of pumps in which rubber bearings were used. They were [190] making deep well turbine pumps, some of them of considerable depth, three and four hundred feet, and they had taken the rubber bearings as the basis of the main patent, and they were advertising the pumps and installing them, and doing a very fine job of selling the pumps, and the pumps themselves were doing a very fine job in the field, especially where sand was being pumped.

Q. As a result of that contact with the use of rubber industrially, did you make any effort to study the subject?

A. I had never heard of rubber being used, of the use of rubber in a rubber bearing, so I went to the library and got what books I could on rubber, and went to a number of rubber companies and talked to some of their men, to make a study of it, in so far as its use industrially was concerned.

Q. After your experience with the Pomona

(Testimony of J. C. Ballagh.)

Pump Company, when did you again come in contact with rubber used industrially?

A. The next time I ran into it was in connection with Mr. Bettis, who was working for the Johnston Pump Company as their engineer, and he had a patent that he had been trying to promote. He had had the patent with the Baash-Ross Tool Company, and with the Emsco Derrick & Equipment Company, and each of them had this patent for about a year, and he told me that they were not doing any good with it, that he had cancelled the Emsco license, and he said he was going to cancel the Baasch-Ross, because they weren't selling any. [191]

Q. How did your experience with the Pomona Pump Company fit in with your meeting with Mr. Bettis?

A. I studied his device, because I would see him when I would come into the office, and he would tell me of his patent, and it occurred to me that the application was very similar, that is, in an oil well there is a long drill pipe that rotates in the well, and in a turbine pump there is a shaft that operates down in the well, and I had seen the Pomona pump handling large quantities of sand and the rubber didn't wear out at all, and I just thought that if that same quality of rubber was put on drill pipe that was in the pump, it certainly might do some good and make some money.

Q. Was the quality of the Pomona Pump rubber a very high quality?

(Testimony of J. C. Ballagh.)

A. I believe it was as high grade rubber as was made at that time. It was very expensive, although there weren't an awful lot of them at that time. They were quite expensive, and it was a very fine grade of rubber. I have never seen a higher grade of rubber.

Q. How did you come to meet Mr. Patterson?

A. Mr. Patterson ran a retread shop in Los Angeles, and for a number of years he had been retreading tires for me, and he made the best retread rubber that I had ever seen, and I got very fine mileage from them. And I had no facilities to make rubber, and I just figured that if I could make some sort of a deal with Patterson to make rubber [192] for me or get it made, I knew if I could get out and make it, that between the two ideas I could probably get into a much better job than I had with the Pump Company.

Q. Did you then form a partnership with Mr. Patterson?

A. I formed a partnership with Mr. Patterson. The two of us made a license agreement with Mr. Bettis, and that was in 1927.

Q. Was the Bettis protector similar to the non-lip protector here?

A. It was a much shorter protector and a larger diameter, but the principle was the same.

Q. Will you describe the first one put on the market, of the new protectors?

A. I was able to borrow one of these molds that

(Testimony of J. C. Ballagh.)

the firm of Baash-Ross had been using, and I told Mr. Patterson to take it over to where he was having his rubber made, and I went over there with him, and I got them to specify the very finest grade of rubber that could be made to work in this mold, and I had them make up about six of them, and I took them down to Long Beach, where the Jergins Trust Company was operated by a man I had known for many years back in Texas, and he gave me permission to put these on a well. And I was able to get them on with a great deal of difficulty, because we yet hadn't developed an expander that was satisfactory. But at the end of two or three days of operating, the protectors were just as good as new; they hadn't worn a [193] bit, and the drillers and superintendent were very enthusiastic about it, and he got permission to buy a whole string of them for the entire pipe.

Q. Prior to that time had the drill pipe been knocking holes in the casing?

A. They had been having trouble constantly with wearing the drill pipe, and also wearing holes in the casing, and there would be water break in, and they were having fishing jobs, and also having a bad time of it, because the wells were very crooked in those days.

Q. Then in March of 1928, I believe, the defendant corporation was incorporated?

A. Yes, sir.

Q. Will you give a short history of the gross sales of the business? A. Up to date?

(Testimony of J. C. Ballagh.)

Q. Yes.

A. Up to date there has been approximately $5,000,000 or more of the protectors sold.

Q. What was the volume? Will you compare the volumes? In other words, was business good when you commenced?

A. Business started out very well. It just happened that I was just starting in the business at a time when drilling was reaching a very high peak, and especially in Long Beach and Santa Fe Springs.

Mr. Lamont: Won't one of your exhibits show this? [194]

Mr. Bednar: No, I don't think so.

Mr. Lamont: I thought you put one in evidence.

Mr. Bednar: I will try to shorten this up.

Q. By Mr. Bednar: Then your sales, I understand, were very good from the beginning down to about what time?

A. If I may refresh my memory on that—the sales reached the peak in 1929. During that year we sold something over $1,111,000, and the following year our sales were $636,000, and they were $149 in 1932.

Q. $149? A. $149,000 in 1932.

Q. Was the Bettis patent declared invalid?

A. The Bettis patent was declared invalid, yes, sir.

Q. About when was it first declared invalid by the trial court? A. In 1931.

Q. After that time did competitors come into the field?

(Testimony of J. C. Ballagh.)

A. Yes; competitors started coming in in great numbers. Some 60 different firms started in the manufacture of protectors during the next three or four years.

Q. When did your company first start manufacturing non-protector items in quantity?

A. In 1932, out of our gross sales of $149,000, our non-protector sales were $100,000, which was retread rubber. Our protector sales had dropped from more than a million dollars down to less than $50,000 during that period, down [195] to less than 5% of our sales, so, in order to keep our crews together and try and keep the organization from disbanding, we went into the manufacture of retread rubber. Mr. Patterson having been in that business, he knew something about retread rubber, so we converted our plant.

Q. How long did this depressed period of gross sales last? A. It lasted until about 1936.

Q. When did you start making and selling non-protector items other than retread rubber?

A. I think our first non-protector items were in 1936.

Q. Other than retread rubber?

A. Other than retread rubber.

Q. And what has been the object of these non-protector items?

A. We were trying to get up a volume of sales of items that weren't tied so closely to the drilling program. The reason our business fluctuated to

(Testimony of J. C. Ballagh.)

such depths, there was no leveling off to keep steady employment.

Q. Did you go into non-protector items for the purpose of leveling out the gross sales, so that they would not depend so much on protectors?

A. We were trying to get into some item, if we could, where there was a larger margin of profit. The price of protectors fell very sharply when the patent was declared invalid, so our margin was very meager, unless we had a large [196] volume.

Q. I understand on your previous testimony you testified that you had a factory in Los Angeles, and you had an assembly plant in Houston?

A. Yes, sir.

Q. Where do you have branch offices?

A. We have a branch in New Iberia, Louisiana; Shreveport, Louisiana; and Vickery, Texas; Ventura, California; Bakersfield, California; Avenal, California; Casper, Wyoming; and in New York City we have an office to take care of our export business.

Q. Do you have an office in Canada?

A. We have no office, but we have an agency and a service station with one of the hydraulic installation developments in Turner Valley.

Q. Just to clear up that point, at all these branches do you keep one of these hydraulic applicators for use in putting these protectors on the drill pipe in that area?

A. Yes; we have one at each one of those stations.

(Testimony of J. C. Ballagh.)

Q. Do you have any stations outside of the North American continent?

A. We have an agency in Trinidad, with a service man that travels through Venezuela and Colombia and Peru.

Q. During this period of time in question did your company sell items destined for places all over the world, that is, until the war came on? [197]

A. Yes; practically our entire line of items were sold in almost all drilling fields of the entire world, where we could sell, with the exception of Russia, where we haven't made any sales for about seven or eight years.

Q. Outside of these service stations you mentioned, do you have agencies in addition?

A. We have agencies with some small stock in many, many locations throughout the area; wherever there was oil well drilling going on, we tried to establish some sort of an agency or service which will be available.

Q. Have you personally traversed, covered the oil fields of the western hemisphere?

A. Yes. I have been in every oil field of any consequence in North America.

Q. Can you estimate, generally speaking, the percentage of protectors in the field during this period of time in question throughout the world, that were sold by your company?

A. I would estimate that we had sold 75%.

Q. How do you make that estimate in the fields outside of the western hemisphere?

(Testimony of J. C. Ballagh.)

A. Outside of the western hemisphere, there are about six or eight companies that do, I would say, 90% of the drilling. That is the Standard Oil of New Jersey; the Royal Dutch Shell interests; the Texas Company; the Socony Vacuum, and the various British firms that have buying agencies in New York; and the Argentine Government. I think that is the [198] most of them, and they buy through New York, first sending out inquiries, and every time there is a protector sale coming up I get a letter from their New York purchasing department requesting a quotation.

Q. And when you don't make the sale in question——

A. We follow it up; if we don't make the sale, we follow it up and find out if we lost it. And quite frequently the order is cancelled. There may be some change in the program. But if the order is not placed we get to know it very soon thereafter.

Q. Are the minutes that have been introduced here in evidence for the period from January 1, 1939, to September 10, 1941, correct to the best of your knowledge and belief?

A. To the best of my knowledge and belief, they are.

Mr. Lamont: I didn't get that question.

Mr. Bednar: I just asked him, were the minutes from January 1, 1939, to September 10, 1941, correct.

Q. By Mr. Bednar: Were you present at the meeting on October 18, 1938, at which Mr. Dulin

(Testimony of J. C. Ballagh.)

moved that you and Mr. Patterson be compensated at the rate of $1500 a month? A. Yes, sir.

Q. And are the minutes of that meeting correct, to the best of your knowledge? A. Yes, sir.

Q. During the period of time in question, can you estimate how much of your time you devoted to the business [199] and affairs of the defendant corporation?

A. I devoted practically all the time during daylight hours to the corporation, and about at least three nights a week I worked at home on my various inventions on which I was working, and writing up my advertising copy, and also making the photographs that we used in our advertising and in our literature.

Q. Have you had a vacation during this period of time?

A. No, I haven't been having vacations.

Q. Have you made a considerable number of business trips?

A. Yes, I have; until Pearl Harbor, I spent at least a third of my time away. In fact at that time I was in New York, at that particular time.

Q. What have been your duties in reference to Patterson-Ballagh Corporation during the period of time in question?

A. Secretary and treasurer, and I acted as sales manager. I had charge of the advertising, the preparation of the advertising copy. I had charge of the various patent litigation that we had in the past, and during that one particular period we had

(Testimony of J. C. Ballagh.)

one case in Oklahoma, and I think we concluded another case in California that we had had running for some time.

Q. Did your company build up a reserve of rubber in view of the international situation?

A. Yes, sir. [200]

Q. When did your company start building that up?

A. About a year prior to Pearl Harbor the Eastern situation looked very dark to Mr. Miller and myself, and we had some cash on hand, and the price of rubber was quite reasonable, and we decided that, rubber being the basis of our business, it was a good time for us to maintain a good inventory. [201]

Q. Whose suggestion was it first that you build up an inventory?

A. I think it was Mr. Miller's.

Q. And, judging from your present stock on hand, on the basis of your doing business in the same manner, under the same policy, that you have done it the last two or three years, how long do you estimate the stock on hand that you have would last you, if the government didn't use it for other purposes?

A. I would say we could stay in business at least a year, or maybe a year and a half.

Q. Has your plant been rebuilt since Mr. Miller came into the business?

A. Yes. It was almost completely rebuilt, and

(Testimony of J. C. Ballagh.)

two new presses installed, and installed a number of new pumps, and our piping has been almost entirely replaced, and installed new rest rooms, and changed our warehouse, and improved our method of handling materials through the plant, changed our stock, making it much more efficient in operation than it was before.

Mr. Bednar: At this point I would like to read from the minutes the duties of the Secretary and Treasurer, from the by-laws. Section 6, appearing on page 24:

"The Secretary shall keep the minutes of all acts and proceedings of the Board of Directors and of the Stockholders done and had at their meetings, in books [202] provided for that purpose; he shall attend to the giving and serving of all notices for the corporation; unless the Board of Directors shall otherwise provide, he shall sign with the President, in the name of the corporation, all bonds, contracts and other obligations and instruments authorized by the Board of Directors, and when authorized by said Board, he shall affix the seal of the corporation thereto; he shall have charge of all records, books and papers pertaining to his office, and the corporate seal of the corporation, the certificate book and such other books and papers of the corporation as the Board of Directors may direct; he shall keep proper books of account and serve all notices required by law or the by-laws of the corporation. With the President or Vice-President, he shall sign all certificates of stock, and he shall in general perform all the duties

(Testimony of J. C. Ballagh.)

incident to the office of Secretary, subject to the control of the Board of Directors. He shall also perform all other duties required of him by law or these by-laws and such as the Board of Directors may from time to time impose upon him. At the expiration of his term of office, he shall deliver to his successor, or such other person or persons as the Board of Directors shall designate, all books and property of the corporation in his possession."

And then the Treasurer:

"The Treasurer shall have charge and supervision of the finances of the corporation. He shall receive, receipt [203] for and safely keep all its funds, and shall dispose of them only in the manner authorized by the Board of Directors; he shall at all times keep a full and complete and accurate record of the funds of the corporation and shall deposit the same to the credit of the corporation in such bank, banks or depositaries as the Board of Directors may designate; he shall, when so authorized by the Board of Directors, sign with the President or Vice-President, or such other person or persons as may be designated by the Board of Directors, all bills of exchange and promissory notes of the corporation. When ordered by the Board of Directors, he shall render a statement of his accounts. He shall at all times be under the control of the Board of Directors, and generally shall perform all duties incident to the position of Treasurer, and all other duties that may be required of him by law, and these by-laws, and that said

(Testimony of J. C. Ballagh.)

Board may from time to time impose upon him, at all times keeping full, complete and accurate accounts thereof. At the expiration of his term of office, he shall deliver all moneys, papers, records and property of the corporation in his possession, or under his control, to his successor, or to such other person as the Board of Directors may designate."

Q. By Mr. Bednar: Now, Mr. Ballagh, I don't believe this chart has ever been explained, and I would like to have you explain it. That chart, incidentally, is Defendants' Exhibit G. [204]

A. This chart represents the sales in 1939, 1940 and 1941 of the three leading non-protector items that are my inventions. It also shows, in the accumulation of the three items, the total, that has been brought up to the 1st of June, showing the continuation of the same steady trend upwards. It shows that during 1938, in the case of the tubing protectors, the sales for the year had been $138.60; at the end of 1939 it had reached $3294.00; at the end of 1940 it had reached $8527.20; and at the end of 1941 it reached $16,691.40.

Mr. Lamont: Gross sales?

A. Gross sales.

Q. By Mr. Bednar: In other words, it doubled each year?

A. Each year it a little bit more than doubled. The sucker rod protectors, the sale in 1938 was $63.00, and $441.00 in 1939, and $1578.50 in 1940, and $2073.50 in 1941. The sales did not quite double in that case. However, in 1940 they had

(Testimony of J. C. Ballagh.)

quite considerably more than doubled. In the sale of the pipe wipers, there was no sale in 1938. There was $12,296.00 in 1939; in 1940 there was $30,189.50; and in 1941 it was $43,862.26, not quite double in that case, but more than double 1939. And I have accumulated the three items together, and have brought in their totals, showing sales in 1938 of $201.60, a rise to $16,232.60 in 1939, and to $56,627.80 at the end of 1940, and at the [205] end of 1941 they were $119,264.90; and in the middle of 1942 they had reached $143,124.10, which is right close to the present time. I put the last period in to show the trend of the three items as still continuing on upwards.

Q. Does your company sell any products at the present time except on priority orders?

A. No. I think everything we sell is on some sort of a rating.

Q. I believe on your first examination you testified that Mr. Armington worked for the company only part time? A. Yes, sir.

Q. How was that?

A. He has a business of his own which he has operated for many years, and which I think he was operating the same business when he started to work for us, if I remember right. I am not quite sure.

Q. What are Mr. Armington's qualifications? What does he specialize in?

A. He is an assistant engineer to me. We call him our engineer. He follows through on the

(Testimony of J. C. Ballagh.)

various devices on which we work. He is out in the field and watches the machines we are running. He watches operations in the plant, and he checks on our costs for us.

Q. Have you had disagreements with Mr. Armington? A. Yes, quite frequently.

Q. Of what nature? [206]

A. But very friendly. We never have anything except friendly disagreements. Oh, a lot of things about the way the business is run, about the duties of certain individuals, about the design of certain of our products, about the pay of some certain persons.

Q. Who first recommended Mr. Burrell to your company?

A. Lyon & Lyon, our permanent attorneys in Los Angeles, who have been doing our patent work.

Mr. Bednar: I am going into these inventions again, your Honor.

Q. By Mr. Bednar: First of all, Mr. Ballagh, I would like to direct your attention to the hydraulic applicator, which is already in evidence here as Defendants' Exhibit J. Are there any parts of a hydraulic applicator present in court here?

A. Yes; there is one transfer sleeve.

Q. Now, with the aid of these pictures which I hand you and the picture which is already in evidence, and this transfer sleeve, will you explain how this hydraulic applicator works?

A. The casing protector is first installed in the hydraulic machine. The protector is pressed over

(Testimony of J. C. Ballagh.)

this shaft, and then this cone is placed over the protector, and then the transfer sleeve is placed over the cone. The transfer sleeve is made so that it will just fit on the edge of this cone. It then stands up in the hydraulic machine as shown [207] in photograph B, I think, part of the same exhibit.

The Court: Have these ever been marked?

Mr. Bednar: May I interrupt for just a moment and have those marked?

The Court: You had better, if you want us to be able to understand the record.

The Clerk: Do you want these marked as one exhibit?

Mr. Bednar: All one exhibit.

The Clerk: They will be Defendants' Exhibit K.

A. The protector starts out a very small diameter and extends to two or three times its size by the pressure of the dog pushing it up, and when it gets on the sleeve, you then turn the latch, and the sleeve, with the protector mounted thereon, can be lifted and carried, so that we can carry a protector mounted. The protector is under terrific tension, and the hole through the center of the sleeve is larger than the tool joint. If this is the tool joint, we can slide it onto the tool joint, onto the drill pipe, anywhere along the pipe that we want to locate it. It is about 30 feet long, and some customers like them in the middle and some near the tool joint, and when we got it to the point we want

(Testimony of J. C. Ballagh.)

it, we take a wrench, that is, two wrenches, and this starts to move, to slip the protector over the edge, and as this starts over the edge, then the pressure starts to release, and that pushes that off and upon the protector, just to the edge. All we need to do is turn this a couple of times, and [208] the protector will pop off, as shown in some of these other pictures. It is a very simple way of putting a protector on. With these large protectors, there will be sometimes six and eight tons of energy stored in that. Then K-1 shows the protector just almost on the sleeve. On K-2 the protector, with the sleeve attached, has been taken away from the machine. In K-3 the protector is slipped over the tool joint.

Q. Let me ask you one question at this time: In K-3, is that a much larger protector than the one we have?

A. No; that will be this same size protector.

Q. The same size as what?

A. It will be, very probably, the same as this protector.

Q. The same as Exhibit C for identification?

A. The same internal diameter, probably one of a little smaller external, but this is a 4-inch tool joint, you can tell by the proportion of it, that it is slid over, and then in K-4 the proector is located or is supposed to be on the tool joint. The man starts to screw the protector off, which he does with a speed wrench, starts to turn it off, and it starts to curl off, and then when he gets over there and he has to hold this sleeve back to keep it from being

(Testimony of J. C. Ballagh.)

thrown back maybe 15 or 20 feet, he has to hold the sleeve. It just throws itself off. In a matter of seconds, it just goes off so fast that it is maybe a hundredth of a [209] second, and it pops off, and you can hear it pop for a quarter of a block, and, as far as I know, it is the only application of rubber where rubber is held in location industrially by its own utility; I know of no other service in any industry that I have ever heard of.

Q. Did you file applications on the hydraulic applicator? A. Yes, sir.

Q. About when were those filed?

A. I think it was in 1939; it was in 1939, on the first application.

Q. Did you file a second application?

A. The second was filed in 1940, in September.

Q. And on the first application did you encounter an interference proceeding? A. Yes, sir.

Q. Was that interference proceeding concluded by cross license agreement between the defendant corporation and the Bettis Rubber Company?

A. Yes, sir.

Mr. Bednar: I have a duplicate original here but it is from the files of Lyon & Lyon, and it is their only copy, and I would like to insert a copy.

Q. By Mr. Bednar: Do you know whether any claims have been allowed on the hydraulic applicator?

A. I don't know. I don't think they have, so far. [210]

Mr. Lamont: No objection.

(Testimony of J. C. Ballagh.)

Q. By Mr. Bednar: Are the applications still being pursued? A. Yes, sir.

Mr. Bednar: I offer a copy of this agreement in evidence as defendants' exhibit next in order, and I might state the substance of the agreement at this time. It is agreed between Bettis Rubber Company and Patterson-Ballagh Corporation—the Bettis Rubber Company also has this other application, that caused the interference proceedings, and each party cross licenses the other party to use the device described in the application, free of charge, with one exception, that in the event that the Bettis Rubber Company uses the mechanical method of slipping the protector off of the transfer sleeve onto the drill pipe, then they must pay Patterson-Ballagh Corporation 25 cents for each rubber protector so placed in position on the drill pipe. On the other hand, if Patterson-Ballagh Company uses the Bettis hydraulic process for transferring the protector from the transfer sleeve onto the pipe, then Patterson-Ballagh Corporation pays 25 cents for each protector so placed in position. Both companies use the hydraulic method for putting the protector onto the transfer sleeve in the beginning. It is only in the method by which the protector is removed from the transfer sleeve onto the drill pipe that the difference exists, and by reason of this agreement the [211] Patterson-Ballagh Corporation uses this hydraulic applicator with the mechanical method of releasing

(Testimony of J. C. Ballagh.)

the protector from the sleeve onto the drill pipe, free of charge.

The Clerk: Is it admitted, your Honor?

The Court: Yes.

The Clerk: Defendants' Exhibit L.

DEFENDANTS' EXHIBIT L

AGREEMENT

This Agreement entered into this 18th day of October, 1940, by and between Bettis Rubber Co. Ltd., a California corporation, hereinafter referred to as Bettis, and Patterson-Ballagh Corporation, a California corporation, hereinafter referred to as Ballagh:

Witnesseth:

Whereas, Bettis represents it is the owner, by an instrument in writing, of the following applications, together with the right to grant licenses thereunder:

Burt S. Minor, Filed August 30, 1937, Serial No. 161,599, for Hydraulic Expander and Applicator for Short Elastic Tubes;

Barnes and Minor, filed February 1, 1939, Serial No. 254,026, for Means for Applying Expansible Collars;

Barnes and Minor, filed July 25, 1939, Serial No. 286,410, for Method and Means for Positioning Expansible Collars on Pipe or the Like;

(Testimony of J. C. Ballagh.)

Aubrey W. Massecar, filed July 26, 1939, Serial No. 286,595, for Method and Apparatus for Applying Protectors to Well Pipe; and

Whereas, Ballagh represents it is the owner of the following applications, together with the right to grant licenses thereunder:

James C. Ballagh, filed May 29, 1939, Serial No. 276,487, for Process and Apparatus for Applying Protectors to Drill Pipe;

James C. Ballagh, filed September 27, 1940, Serial No. 358,701, for Process and Apparatus for Applying Protectors to Drill Pipe; (This is a divisional application of Serial No. 276,487); and

Whereas, said application of Bettis, Serial No. 254,026 is at present involved in an Interference No. 78,231 with said application of Ballagh, Serial No. 276,487; and

Whereas, Bettis has moved to add to said Interference No. 78,231 its other applications Serial Nos. 161,599, 286,410 and 286,595, and

Whereas, the aforesaid applications of both Parties will undoubtedly be involved in said Interference No. 78,231, or other interferences to be declared, and

Whereas, it is the desire of the parties hereto that an agreement be entered into, whereby, Interference No. 78,231 may be terminated, the declaration of other interferences be prevented, patents is-

(Testimony of J. C. Ballagh.)

sued on said applications to the Party having priority of invention as to the various claims contained therein, and said Parties shall both have rights under the respective applications or patents to be issued thereon;

Now, Therefore, in consideration of the mutual covenants of the parties as hereinafter expressed, the parties hereto agree as follows:

I.

Said parties shall examine or cause to be examined the said applications of the respective parties, securing all information as to dates of conception, reduction to practice, etc., and shall thereafter determine what application shall be given priority in Interference No. 78,231.

II.

In case any of the remaining applications hereinabove identified and not involved in said interference, or any of the claims thereof, conflict, a determination shall be made from said examination as to what applications have priority and to whom a patent for the inventions disclosed therein should be issued; all possible means shall be taken to eliminate conflicts in the Patent Office and to assure that patents are issued upon the applications which have priority of invention.

III.

That the parties shall execute concessions of priority or any other documents or papers necessary

(Testimony of J. C. Ballagh.)

to terminate said interference, and to cause patents upon said applications to be issued to the parties who shall have been determined to have priority of invention.

IV.

Bettis grants to Ballagh and Ballagh grants to Bettis a personal, nonexclusive license under the aforesaid applications and patents to be issued thereon to manufacture and use in the United States and to sell for use in foreign countries, hydraulic devices and means and applicators for enlarging the inner periphery of elastic protectors for the purpose of placing the same upon members of larger diameter, whether said members be drill pipe or transfer sleeves, and also to employ for the same purpose any and all methods claimed in said applications or contained in patents to be issued thereon except that any license granted in this agreement to Ballagh shall not include the right to use a follower or pusher rubber behind the protector to be applied.

V.

Bettis grants to Ballagh under said applications of Bettis and any patents issued thereon a personal non-exclusive license to manufacture and use in the United States and to sell for use in foreign countries transfer sleeves as disclosed in any of the hereinabove identified applications which embody mechanical, as distinguished from hydraulic means, for removing the protectors from such sleeves to drill pipe or the like, and Bettis agrees not to use

(Testimony of J. C. Ballagh.)

any such transfer sleeves as licensed in this paragraph except as otherwise herein provided.

VI.

Ballagh grants to Bettis under said applications of Ballagh and any patents issued thereon a personal nonexclusive license to manufacture and use in the United States and to sell for use in foreign countries transfer sleeves as disclosed in any of the hereinabove identified applications which embody hydraulic, as distinguished from mechanical means, for removing the protectors from such sleeves to drill pipe or the like, and Ballagh agrees not to use any such transfer sleeves as licensed in this paragraph except as otherwise herein provided.

VII.

That any and all patents acquired by the Parties hereto covering any improvements on the devices or methods of said applications shall be within and covered by the licenses granted herein.

VIII.

That the parties hereto shall have the right and license, by written request to employ the mechanical and hydraulic means reserved to the other party in Paragraph V and VI hereof upon the payment of a royalty of Twenty-five Cents (25c) for each and every protector installed by said mechanical or hydraulic means in effecting the removal of an elastic protector to a drill pipe and the like

(Testimony of J. C. Ballagh.)

from a transfer sleeve; that any party exercising said right and license in this paragraph granted shall keep a true and accurate account of the number of protectors sold under the provisions of this paragraph and to whom sold and shall submit a statement in writing by the 25th of each month covering the number of protectors so installed during the preceding month's operations, together with a check in payment for said royalties; and the other party shall have the right, upon reasonable notice, at reasonable times to examine the books of the other for the purpose of ascertaining the accuracy of said statement. The right of examination, however, shall not extend to other books or records than those specifically covering the installations and sale of protectors as in this paragraph provided.

IX.

That the licenses granted herein shall be non-assignable by either party except that they shall be transferable to the successor in interest of the business of either party.

X.

That the party who is the owner of any patent issued upon said applications shall have the right to determine what suits for infringement thereof may be instituted or conducted and shall bear the cost thereof, including fees of attorneys engaged by it, provided, however, that the other party shall have the right to be represented by counsel where

(Testimony of J. C. Ballagh.)

said counsel is paid by said other party; it being the intention of the parties hereto that they shall cooperate in connection with any infringement actions which may be brought in order to establish the validity and infringement of any patents in issue.

XI.

This agreement shall continue in force and effect until the expiration of the last patent to be granted upon the applications specified herein, unless otherwise mutually terminated by the parties or as hereafter provided for.

XII.

This agreement may be cancelled by a notice in writing for any material breach hereof unless the other party, within thirty (30) days thereafter, cures said default.

XIII.

Bettis shall have the right to purchase and Ballagh agrees to sell to Bettis, at cost, mechanical applicators covered by United States Patent No. 1,965,876 for use abroad but not for use in the United States. This right is personal to the parties hereto.

(Testimony of J. C. Ballagh.)

In Witness Whereof, the parties hereto have affixed their hands and seals the date first above written.

BETTIS RUBBER CO., Ltd.
By B. H. BARNES
President
PATTERSON-BALLAGH CORPORATION
By J. C. BALLAGH
Sec-treas

[Endorsed]: Filed July 3, 1942.

Q. By Mr. Bednar: Have you conducted tests in the field to determine whether or not the method used by the Bettis Rubber Company for releasing the protector from the sleeve onto the drill pipe is faster or slower than your mechanical method?

A. Yes, sir, I have.

Q. What have been the results of those tests?

A. We have been considerably faster in our installation.

Q. What is the importance of that?

A. That means that the crew making the installation is freed from staying on the job so long, first, and in the second place, if some of the crew are helping make the installation, it frees them. In cases where there are a large number of protectors, three or four or sometimes five hundred, the difference of just a matter of a few seconds to each

(Testimony of J. C. Ballagh.)

protector may make a difference whether a man has to stay all night on the job or come back the next day, if he can install them all in a few hours time and the men can finish them.

Q. Without a hydraulic applicator of the form your [212] company now has, can you estimate what would happen to your sales of protectors?

A. I think they would be very materially less, very much less, except for export.

Q. Why is that?

A. We have never sold the hydraulic machine outside of the United States yet. These protectors installed outside of the United States don't use the hydraulic method. That would affect our sales only in the United States. It would very materially affect our sales in the states, very materially.

Q. Before you had your hydraulic applicator, did you lose customers by reason of the fact that somebody else had a similar device?

A. Yes, sir; we lost a great percentage of our business.

Q. Who had the other device at that time?

A. The Bettis Rubber Company. They had a hydraulic applicator. They didn't use a transfer sleeve at that time. They installed it direct on the rig. But with the hydraulic method it is much faster.

Q. You were using a manual applicator when Bettis came out with the hydraulic applicator?

A. Yes.

Q. But without the sleeve?

(Testimony of J. C. Ballagh.)

A. Without the sleeve. We developed the sleeve, which was a big advance over their system. We were able to [213] make installations on the rig, away from the rig. We have made installations hundreds of miles away from the rig itself.

Q. What is the importance of that?

A. The importance of that is that there is no well time lost at all. And we can go in the yards where the pipe is stacked, and we will have days of time to make installations, days to pick out just the joints of pipe on which they want the installation to be made, and we can come there at our pleasure and make the installation. And it also allows the protector to be put anywhere along a full length of a drill pipe. Many companies like to put the protector in the middle of the joint. Some like to have it five feet from the end, and some people like to have it within a foot of the end, and we are able to put it where they wish.

Q. When you speak of a tool joint, do you mean a whole length of drill pipe?

A. No. I mean the joint that is on the end of the full length of drill pipe, just the connection between one length of drill pipe and the next.

Q. I refer you to Defendants' Exhibit B, and ask you whether or not you have portrayed on that exhibit the effect of the hydraulic applicator on the application of these protectors to the drill pipe? A. Yes, sir.

Q. What does that indicate?

(Testimony of J. C. Ballagh.)

A. It indicates that in 1939 approximately 7 percent of [214] all protectors that we sold were installed by the hydraulic method. In 1940 it was 36½ percent, and in 1941 it was 47 percent.

Q. Do you have any customers who, after having used the hydraulic method, have reverted to the other method? A. Yes, sir.

Q. In what states?

A. In California we have had the Union Oil Company and the Associated Oil Company and the Shell Company.

Q. I believe you misunderstood my question. Have you ever had a customer which, after having used the hydraulic method for placing these protectors on the drill pipe, has thereafter gone back to the old manual method?

A. Never in the history of our business.

Q. Under what circumstances is the old manual applicator still used?

A. The old manual method is used in export and in locations in the Mid-Continent, where they cannot be reached readily. There are locations where they are drilling on barges out in the Gulf, and up in North Dakota and Michigan and Mississippi, where it doesn't pay us to send over a man with a hydraulic machine, and we therefore are able to send them a few protectors with the old style expander, and he uses it and makes the installation, and then returns the tool to us.

Q. When your company sells protectors does that include [215] the service?

(Testimony of J. C. Ballagh.)

A. We sell every protector installed, except those sold for export.

Q. After your company started using hydraulic applicators, did they obtain new customers on that account? A. Yes, sir.

Q. What customers are those?

A. Many customers in the Mid-Continent, and, more specifically, in California, the Associated Oil Company, the Shell Company, the Union Oil Company, the Barnsdall Company, Richfield, Belridge Oil Company, The Texas Company.

Q. Is this device for sale? A. Yes, sir.

Q. To the public? A. Yes, sir.

Q. Have any of them ever been sold?

A. No; we never have.

Q. Is there any other competition in respect to this device other than the device used by the Bettis Rubber Company?

A. The Grisly Manufacturing Company have a hydraulic applicator. There is one being used in Oklahoma.

The Court: I think we will suspend here until 10:00 o'clock Monday morning.

(An adjournment was taken until Monday, July 6, 1942, at 10:00 o'clock a.m.) [216-17]

Los Angeles, California,
Monday, July 6, 1942. 10:00 A. M.

(Present as before.)

The Court: You may proceed.

Mr. Bednar: Mr. Ballagh.

J. C. BALLAGH

(Recalled)

Direct Examination
(Resumed)

By Mr. Bednar:

Q. Mr. Ballagh, has there ever been any contract between you and Patterson-Ballagh Corporation requiring you to spend your time inventing?

A. No, sir.

Q. Has there ever been any such contract as to Mr. Miller? A. No, sir.

Q. Has there ever been any contract between you and Patterson-Ballagh Corporation requiring you to assign any of your inventive rights or patents to the corporation? A. No, sir.

Q. Has there ever been any such contract as to Mr. Miller? A. No, sir.

Q. In what countries of the world has your corporation sold its products?

A. In Canada, Mexico, Cuba, and the Dominican Republic. [218] Trinidad, Venazuela, Colombia, Peru, Brazil, Argentine, Australia, New Zealand, Borneo, Dutch East Indies, Japan, Burma, China, Persia, Turkey, Egypt, Roumania, Iraq and Iran, Austria, Germany, England, Russia, the Belgian Congo, Alaska, in the United States; I think in Italy, Persia—I think I have named that. I think that is approximately the list.

Q. Mr. Ballagh, I refer you to Plaintiff's Exhibits 5-A, -B and C, which are the Pennington audits. Were copies of those audits sent to Mr. Dulin

(Testimony of J. C. Ballagh.)

within a short time after they were published by Mr. Pennington?

A. Yes, sir; they were, very shortly thereafter.

Q. In other words, Plaintiff's Exhibit 5-A, for the year 1939, is dated by Mr. Pennington March 29, 1940, and within a short time thereafter a copy was sent to Mr. Dulin? A. Yes, sir.

Q. And the same is true of the other audits?

A. Yes, sir.

Mr. Bednar: At this time I would like to read into the record a short portion of the minutes of the annual meeting in January of 1942.

Mr. Lamont: What is the materiality of that?

Mr. Bednar: You are complaining of certain actions taken in 1941, and this has to do with the ratification thereof, at the end of the year.

Mr. Lamont: All right. [219]

Mr. Bednar: Do you want to check my reading here?

Mr. Lamont: I would like to check it afterwards.

Mr. Bednar: It appears from the minute book that all shareholders were present in person or by proxy, including Mr. Dulin.

"Ratification of prior acts of officer and directors.

"The suggestion was made that the meeting consider the matter of the adoption of a resolution ratifying and approving the action of the Board of Directors and the acts of the officers of the company, since the last annual meeting of the shareholders. E. S. Dulin stated that he opposed the

(Testimony of J. C. Ballagh.)

adoption of such a resolution for the reason that the officers and directors had taken action and performed acts during the period not consistent with the best interests of all the shareholder and that the Board of Directors had taken action during the period in respect to the fixing of salaries and the payment of additional compensation after a consideration of interim statements which, in his opinion, did not correctly reflect the condition of the corporation in so far as its actual earnings and condition were concerned.

"Thereupon, on motion of H. C. Armington, seconded by Howard Burrell and carried, E. S. Dulin voting in the negative, it was

"Resolved, that all action taken by the Board of Directors of this Corporation since the last annual meeting of the shareholders thereof, whether said directors were de [220] facto or de jure, and all acts of the officers of this corporation done pursuant to the authorization of the Board of Directors or with the knowledge and acquiescence of the Directors are hereby ratified, approved and confirmed as and for the corporate acts of this corporation."

Q. By Mr. Bednar: Mr. Ballagh, when did you begin a course of developing inventions and new devices of your own? A. About 1938.

Q. And what was the device that you started out on?

A. The hydraulic applicator.

Mr. Lamont: The what?

(Testimony of J. C. Ballagh.)

A. The hydraulic applicator.

Q. By Mr. Bednar: Prior to 1938 the patents and inventions and new devices used by your corporation were developed by somebody other than yourself? A. Yes, sir.

Q. I believe in the last testimony on Friday you were just concluding on the hydraulic applicator, and I am going to ask one more question on it. How much saving of time is there in the use of the hydraulic applicator over the manual applicator, time and expense?

A. In the drilling of extremely deep wells, in which our protectors are sold, and in which the majority are sold, there is a saving to the operator of direct time of from 35 to 40 hours during the installation of the protector, and there is an additional saving of at least that much time, [221] generally somewhat more, in the time that is otherwise lost in going back into the hole and redrilling and getting back to bottom. And then when they are back on bottom they have to circulate for a much longer period of time to get the mud back into condition, if they have been out of the hole for any length of time. For each hour that they are out of the hole, they probably spend 30 minutes of circulating mud, that is, in the deep wells, where the big majority of our protectors are sold.

Q. Can you estimate the saving per hour, for example, to the operator?

A. The big rigs that drill these deep wells, the

(Testimony of J. C. Ballagh.)

time runs from 120 to 125 feet an hour. They call that the well time, and there is probably 40 hours direct time, and at least 40 hours indirect time, and maybe 50 to 60 hours indirect time, a total of maybe 100 hours altogether during the drilling of the well.

Q. Have you assigned your two applications in reference to the hydraulic applicator to the corporation? A. Yes, sir.

Q. Passing onto the lip protector, you, I believe, testified that you were the inventor of that?

A. Yes, sir.

Q. And an application has been filed for patent?

A. Yes, sir.

Q. Has there been a conveyance to the corporation of [222] any rights that you may have in that?

A. Yes; I assigned all my right and title to it.

Q. What is the function and purpose of the lip on this protector?

A. The lip protector is to prevent the swirling of the mud that occurs above the protector in the old style. There is a little ledge above the protector, where the protector extends outward from the drill pipe, and there is a swirling effect, due to the velocity of the mud. The mud has sand in it that causes a swirling, and that acts on the drill pipe, and there takes place an action that is known as cavitation, cavitation and a sandblasting effect, very probably a combination of both of them, in which part of the metal is removed, and that leaves a groove just above the protector, and that groove gets deeper and deeper, and as soon as it gets seri-

(Testimony of J. C. Ballagh.)

ous, then the drill pipe has to be laid aside; otherwise it will break; and in many cases, where they don't notice that, the drill pipe would break, causing a very serious fishing job.

Q. Are you acquainted with any fishing jobs that cost a substantial sum, on account of the pipe grooving under the use of the old protector?

A. I wasn't on the jobs where they had the fishing, but our salesmen have told us of a number of instances where jobs have cost several thousand dollars.

Q. What has been the effect of the lip protector on the [223] slipping of the protector up and down the pipe?

A. The lip protector has approximately 15 ercent greater area in contact with the pipe, and the resistance to slipping depends directly in proportion to the area that is in contact with the pipe. The longer the protector the less the tendency to slide.

Q. What has been the experience of the company as between the two types of protectors, in respect to the matter of tearing and ripping the protector in applying it to the pipe?

A. The loss due to torn protectors is almost zero at the present time. We had losses of two or three percent in the days before we used the lip protector, and the reason for that was that when the tearing takes place in the old style protector the tear starts in the body of the protector, and it continues on down, and gradually gets bigger and

(Testimony of J. C. Ballagh.)

bigger, as the protector is under a heavy stretch. In the lip protector the tear starts on the lip, and when it reaches the body of the protector itself it will stop. The body of the protector becomes thicker, and when the tear reaches the body it stops. So the lip may be torn, but the protector is not damaged.

Q. Has your company, after engaging in the sale of these lip protectors, ever had a complaint that the pipe was grooving?

A. We have never had a complaint since that time, and [224] our salesmen tell us that the lip protector has entirely cured that situation ever since we started using the lip protector. In fact, of our many customers that we now have, they won't accept the old style protector. We have had many cases in which they sent them back to the plant, and many of them gave us an order and they specified on the order that they must have lips.

Q. Have you ever had any customers who have used the lip protectors who requested the old protectors? A. We never have.

Q. Can you estimate the average cost of labor and material going into a lip protector?

A. It would be the same as making a standard protector.

Q. Approximately what is that?

A. Well, it would depend entirely on the size. We make different sizes, and each one, of course, has a different weight and time.

(Testimony of J. C. Ballagh.)

Q. Are you in a position to estimate the average cost of labor and material on that?

A. The average weight of all protectors I would say is about eight pounds to the protector, and we estimate a labor and material cost of about $2.50 for the labor and material, so that it does not make any difference to us whether it is lipped or unlipped, as far as our manufacturing cost is concerned, with the exception that when we would change over from the standard protector to the lip protector, we would [225] have to make additional molds for the design.

Q. Do you still sell the old type protector?

A. Yes; we still have them, if they want them.

Q. What is the average retail price on a protector?

A. About $8.00; $8.00 or $8.50 would be the average of all sizes.

Q. What sort of competition do you have in the sale of lip protectors? Is there any competing device?

A. We have none. As far as I know, there is no competing device on the market.

Q. Except the old rubber style protector?

A. Yes,—no competition with the lip protector.

Q. Your company is the only company putting out the lip protector? A. Yes, sir.

Q. Can you describe the prospects in respect to the lip protector?

Mr. Lamont: That is asking for the opinion and

(Testimony of J. C. Ballagh.)

conclusion of the witness, if the Court please, and I object to it.

The Court: I don't know. What do you have reference to?

Mr. Bednar: The future. In some of these devices the future is not so good.

The Court: These are all made of rubber, and I don't think the future looks so good for any of them.

Mr. Bednar: Probably not, except that they have a year and a half's supply. [226]

The Court: Well, then it would look good for a year, probably.

Q. By Mr. Bednar: I now refer you to Defendants' Exhibit A, and ask you whether or not the area shown, referring to the lip protector, correctly reflects the gross sales in respect to them.

A. Yes, sir, in 1941.

Q. And in 1940?

A. 1940, 70 percent lip protectors.

Q. And there were none sold in 1939?

A. No. There was a few sold. Our first experiments were made in 1939, and customers paid for those.

Q. Now passing onto the drill pipe wiper, I understand that the previous time you were on the stand you testified that that was your invention, and that patent has been obtained and assigned to the corporation, and I believe the patent is in evidence? A. Yes, sir.

(Testimony of J. C. Ballagh.)

Q. What is the approximate manufacturing cost of the average pipe wiper?

A. I think our average of all sizes made last year was about $5.75, labor and material.

Q. What is the average retail price?

A. $31.00 average.

Q. Will you describe briefly the object and purpose of the pipe wiper? [227]

A. In the drilling of an oil well the drill pipe is rotated vertically, and at the bottom of the well is a bit and mud is circulated to carry away the cuttings. This mud is a very thick and very heavy mud, and in many cases very expensive. When the drill pipe is pulled or withdrawn from the well, the mud adheres to it, and in ordinary practice they use a stream of water to wash the mud from the drill pipe back into the hole. But adding this extra water means that there is a dilution of the mud, and in order to operate efficiently mud weighting material must be added to the mud, so as to bring it back up to the standard required consistency. Also there is considerable time used in the mixing of this mud and getting it back into the well, so that as the pipe is withdrawn there is added extra water, and there is added mud weighting material, which means added material, both material and water, that is used. In the wintertime this water that is added or the mud that is left on the pipe, freezes, and it is very disagreeable in the areas where there are freezing conditions.

(Testimony of J. C. Ballagh.)

Q. After the dilution of the mud weight material with water, if more mud weight material isn't added, what happens?

A. The mud is then thinned, and there would be a blowout. There have been a number of blowouts where the balance between the pressure of the bottom of the well and the weight of the mud is destroyed by the dilution of water, and those blowouts are extremely dangerous and very, very costly. Some of them [228] have cost hundreds of thousands of dollars and destroyed the entire well. Then there is an added danger in working around a well which is open, and tools are frequently dropped down the hole and fall in the bottom, and occasionally very expensive fishing jobs are necessary. With the advent of the drill pipe wiper the use of water for washing is abandoned. They add extra mud or extra water, and the operations at the rig are much safer, and with the pipe wiper covering the hole, the tools that might otherwise drop down the hole are no longer a danger to the well. There is also the factor of the inspection of the pipe. The pipe is wiped clean, and any slight leak can be found, and can be found before it can be a danger to the well.

Q. In other words, holes and abrasions on the pipe can be discovered before the pipe is put back into the well?

A. Yes. In the pulling of casing from wells and the pulling of drill pipe, the oil would cover the tubing or the drill pipe, and this oil covers the

(Testimony of J. C. Ballagh.)

whole rig and makes it dangerous for the men to work around there. It is very slippery and it slows up the operation, and there is a very grave fire hazard. If oil spreads all over the floor from the drill pipe, it picks up any extra dirt there is on the ground, when they lay the drill pipe or the tubing down, and makes a very difficult job. It makes a very great saving in operations where they are pulling tubing that is covered with oil, especially with thick, viscous oil. [229]

Q. How do your protectors that are on the drill pipe get through the pipe wiper?

A. The pipe wiper has a thin web, and the protectors go right through it.

Q. The inner part of it is more resilient than the outer part?

A. Yes; it will stretch, and the protectors go right on through it.

Q. Is there any competition in this field?

A. Very little. There was one company that started the manufacture of wipers, and, as far as I know, they have abandoned the manufacture. I haven't seen any for close to a year. As far as I know, there is no competition.

Q. Can you estimate the approximate percentage of your devices in the field, your pipe wipers, in the field, as against pipe wipers put out by other people?

A. I would say it is at least 99 percent.

Q. Sold by your company?

(Testimony of J. C. Ballagh.)

A. Yes, sir. I don't know of any competing device in service at the present time.

Mr. Bednar: At this time I would like to offer in evidence a picture of the pipe wiper, without the printing that is on there.

The Clerk: Defendants' Exhibit M.

Q. By Mr. Bednar: Directing your attention, Mr. Ballagh, to Defendants' Exhibit G, and to figure 3 thereon, [230] does this graph correctly represent the gross sales of pipe wipers in 1939, 1940 and 1941? A. Yes, sir.

Q. And are these figures on the graph cumulative? In other words, let me put it this way: Were the sales in 1931, the gross sales, $12,296.00?

A. Yes, sir.

Q. And were the gross sales in 1940, $30,189.50?

A. 30 cents.

Q. $30,189.30? A. Yes, sir.

Q. And were the gross sales in 1941, $43,862.20?

A. Yes, sir. They are not cumulative. In other words, those three years would be the adding of those three years together.

Q. In respect to the Kelly Wiper, Mr. Ballagh, is this another device that you manufacture under your pipe wiper patent?

A. This is the larger size pipe wiper. That is a slightly different design than the other pipe wiper. This is a pipe wiper that we designed as a result of a request of the Humble Oil & Refining Company to provide one with windows in which they

(Testimony of J. C. Ballagh.)

could watch their mud level. This is what we call our 19-inch pipe wiper.

Q. That is not the Kelly Wiper?

A. No, sir. [231]

Q. Is that the Kelly Wiper?

A. Yes, sir; that is one of the designs of the Kelly Wiper, and this second device is another style, made in three or four different styles to fit different kellys of different manufacture. They all represent the same principle, that is, being a rubber web that wipes the kelly in the same manner that the drill pipe wiper wipes the drill pipe. The purpose of the Kelly Wiper is to keep the mud from getting into the roller bearings of the kelly.

Q. Will you explain what the kelly is?

A. The kelly is the driving device of an oil well. The drill pipe itself is round, and the rotation is transmitted to the drill pipe by means of a square bar that has an up and down movement, and at the same time can be driven horizontally, and as it moves up and down, of course, the lower part gets into the mud, and it drives through a housing in which are located roller bearings which just fit the square.

Q. Will you refer to that by the page and number of the exhibit?

A. This is the inside cover.

Q. Of Defendants' Exhibit E?

A. The drill pipe fits onto the bottom of this kelly joint. The kelly is the steel housing which operates the kelly portion. The wiper is attached to

(Testimony of J. C. Ballagh.)

the bottom of this housing. Various manufacturers have different designs, [232] so we have made various styles of housing which fit to their design. In this particular design, this steel housing would be just at the lower part of this housing. Another design would be at the bottom, in the same manner; it would be possibly welded in the housing, and later on, when one of the rubbers wear out, they can undo all the bolts or unscrew the bolts, and put in a new rubber or new wearing medium.

Q. When were these Kelly Wipers invented?

A. In 1940.

Q. Who invented them? A. I did.

Q. Has an application been filed?

A. No, not as such. It will be a patent, I think, that will issue subject to the original pipe wiper patent, because it has got the same type of construction, except that it has got a square hole instead of a round hole.

Q. Has there been any assignments of rights in respect of the Kelly Wiper?

A. Yes, sir, along with the pipe wiper.

Q. What is the approximate cost of manufacturing, labor and material, in respect to a Kelly Wiper?

A. $8.00 for the average of those that were sold last year.

Q. And what is the approximate retail price?

A. The retail price of the assembly was $23.10.

Q. I will show you Defendants' Exhibit A, and indicate [233] thereon, in 1941, Kelly Wipers,

(Testimony of J. C. Ballagh.)

$1039.50. Are those the wipers you are referring to?

A. Yes, sir.

Q. And there were none sold in 1940?

A. I don't believe there were any sold at all in 1940.

Q. Are there competing devices in the field?

A. No, none, none that I have ever heard of.

Q. Has all the experimental work on this been done?

A. Yes, sir, I think it has. We made our patterns and had the machine work standardized, and made the jigs, and made the molds.

Q. Has this item been pushed in 1941 by your corporation? A. No; very little.

Q. Why was that?

A. The steel used in it is almost impossible to get under the rating that has been assigned to the oil industry. They were assigned an A-8 rating in the oil industry, or except in certain cases, and we can't buy steel under an A-8 rating at the present time.

Q. Now turning your attention to this plastic tubing protector, are there any other examples of this device in court except this one?

A. Yes; there are two others.

Q. Will you explain the nature and purpose and function of this device? [234]

A. After an oil well starts dropping off in production from its initial flow, the well is then started operating by a pump, and most of the pumps made are sucker-rod pumps that operate inside of tubing,

(Testimony of J. C. Ballagh.)

and in the pumping wells there is a pulsation reaction of the tubing against the weight of the fluid. Each time the sucker rod and the pump moves upward, the pump itself will move slightly downward, due to the extra weight, and that pulsation is up and down, and the collar is in contact with the casing, a very close fit, and as time goes on the collar pulsating up and down against the casing starts to wear the casing so it will split or crack, and it will wear out. That is the effect of the wear, without any device to prevent the wear. It is a very common occurrance in the oil fields.

Q. Who is the inventor of this plastic tubing protector?

A. The first ones were made without any invention. We took a standard piece of plastic and impregnated the canvas, in 1934 or 1935, and we made the device that is shown here. That worked quite satisfactorily, and we sold many of them, but they wouldn't stand up very well; they would wear, and when they would come out of the hole they would have to be replaced, not all of them, but many of them.

Q. When did you begin to sell those?

A. I think in 1935 or 1936, the very first ones. We experimented with them in a small way for a couple of years before we started making any great number, and after this [235] device was going we found this trouble, and then I worked on a new type of material, which I have in this sample, made

(Testimony of J. C. Ballagh.)

in another manner and from other materials and different molding.

Mr. Bednar: This last one I would like to introduce in evidence as an exhibit for identification.

The Clerk: It will be Exhibit N for identification.

Q. By Mr. Bednar: Has there been any application for patent on Exhibit N for identification.

A. No, sir, not yet.

Q. Is it a secret process?

A. It is a secret process at the present time.

Q. When did the sales of Exhibit N commence?

A. I think we made our first sales in 1938. There were very, very few of them.

Q. I mean of this new one, not the old type?

A. I think in 1939 the first sales were made of the——

Q. I show you Defendants' Exhibit G, and refer you to figure 1 appearing thereon. Is that the new style of tubing protector, Defendants' Exhibit N for identification?

A. Yes. We were working on both those designs at that time, both the old and the new, and various other combinations.

Q. And are the figures representing the gross sales on that cumulative, or do they represent each separate year?

A. They are each year by year, the sum total of three years, and a fraction thereof would be added together to form the total for the period. [236]

Q. What is the estimated average cost of one of

(Testimony of J. C. Ballagh.)

these tubing protectors, cost of manufacture, labor and material?

A. Last year the average of all we made was $3.25.

Q. What is the average retail price?

A. $6.60.

Q. Is there any competing device in the field?

A. No, not at the present time. Several years ago one firm started making a competing device, but they abandoned manufacture.

Q. Has the performance of Defendants' Exhibit N for identification been a marked improvement over the old tubing protector?

A. Yes, it has. As far as I know, we have never had one of the new devices worn out.

Q. What are some of the qualities of this new plastic material?

A. It prevents the rubbing of the steel against steel in the well, as the well pulsates; it is lighter than the steel, so any cuttings from it will float out with the oil, and by reducing the friction it makes pumping easier, and it makes it easier on the rods, and cuts down the cost of the fishing jobs which are caused by the tubing wearing out and the very expensive job of cementing the holes that are worn in the casing by the collars when those are used.

Q. Is the material oil proof?

A. Yes, it is oil proof. It is also electrically [237] proof. It cuts down the electrical action of the brines that are in the oils, that ordinarily eat the pipe.

(Testimony of J. C. Ballagh.)

Q. Is this the first non-rubber item that your corporation has engaged in selling?

A. Yes, I think it was the very first.

Q. Are experiments now being conducted for the use of that material in other fields?

A. Yes, sir. We are experimenting with its use in aircraft work, and some for marine and other industries.

Q. What has been the reaction of the oil trade to this new departure?

Mr. Lamont: I object on the ground that it asks for a conclusion of the witness.

The Court: Overruled.

A. In oil fields where the pumping is deep enough to have this trouble occur it has been of tremendous help to those operators. Many wells that formerly weren't able to operate because of the excessive cost of operating, have started pumping again, and wells that have had thousands and thousands of dollars of cost of plugging the holes caused by the wearing of collars, and that has been entirely eliminated. In some certain fields, we have got as many as 3000 in one field, and in one field we have them on every pumping well, and in one field in North Louisiana, and one certain field in Mississippi, they are on every well that is being completed. [238]

Q. Is there any method of estimating the saving to the operator of the plastic tubing protector?

A. I don't think I could make any estimate of saving. I know one company in Northern Louisi-

(Testimony of J. C. Ballagh.)

ana, where their superintendent told me that they spent $30,000 in five wells, having them repaired, before they started using these protectors, and they have used the protectors for more than a year, and he said they had never had a repair job since. What that would figure per barrel I have no way of knowing.

Q. Now, whose invention is this plastic sucker rod protector?

A. There are two different styles of plastic sucker rod protector. One is the box style, and the other is the rod style.

Q. Limit yourself to the box style for the present.

A. The box style is very similar construction to the tubing protector, the same type of ring and the same type of application on the tubing collar with the sucker rod box.

Q. In other words, the material on the sucker rod protector is the same as on Defendants' N for identification? A. Yes, sir.

Q. Who is the inventor of the box style sucker rod protector? A. I am.

Q. Has there been an application for a patent?

A. No, sir, not yet. [239]

Q. What is the function and purpose of that? What is a sucker rod?

A. A sucker rod is a rod that is used to actuate the pump at the bottom of a pumping well. The rod is slowly pulled up and down, and the valve at

(Testimony of J. C. Ballagh.)

the bottom of the pump closes on the upstroke and opens up on the downstroke.

Q. Why is it necessary to have a protector?

A. The wells are very seldom straight. They are crooked; and as the rod goes around corners it wears, event the rod itself, or tubing, or both. The plastic protector on the outside of the box contacts the inside of the tubing and acts as a wear medium between the two.

Q. What is the average cost in labor and material of a sucker rod box style?

A. $1.50 was the average last year.

Q. What is the average retail price?

A. $5.50.

Q. Now referring you to Defendants' Exhibit G, figure 2, does that correctly portray the volume of gross sales of sucker rod protectors, box style, from 1939 to 1941? A. Yes, sir.

Q. And the yearly figures appearing thereon are not cumulative, but they represent the figures for the particular years in question?

A. Yes, sir. The sum total of those would be the cumulative figures. They are the annual sales.

[240]

Q. Incidentally, if a patent of any kind is issued to you on this new plastic material, is it your intention to assign it to the corporation?

A. Yes, sir.

Q. Are there any competing devices for this box style sucker rod protector?

(Testimony of J. C. Ballagh.)

A. Yes, sir. There are quite a number. There are devices made of wood, devices made of bronze, and lead, and babbit, and made of steel, of various shapes. It is one of the toughest problems there is in the operation of an oil well, and probably one of the most serious, and many have tried to solve it.

Q. Now passing to Mr. Miller's inventions, I just want to bring this out. Your Honor will recall in the prior testimony that both of these wire line wipers were patented, and have been assigned to the corporation. Will you please tell us very briefly the function and purpose of these wire line wipers, Mr. Ballagh?

A. In drilling an oil well they use a wire line when they pick cores and when they have fishing jobs and have trouble with the bits. It is used when the drill pipe is out of the hole, ordinarily, although there are coring devices for the wire line going down inside of the drill pipe. In the withdrawing of this wire line from the well mud adheres to it. In the drilling of the well mud or oil adheres to it, if the well is on production. As the wires comes out of the [241] well the mud is thrown off or blown off, and it covers and drops on the machinery and drops on the pipe and drops on the men, and it it is oil, it will be a very fine spray of very inflammable fluid, and many fires have been started in rigs by the oil spray, mud or oil getting on the floor and making it difficult for the men to work safely and rapidly. But the problem I have solved is all to the advantage of the operator. It

(Testimony of J. C. Ballagh.)

doesn't save very much in the way of oil or mud; it saves a little bit, but not very much. Its biggest saving is in the safety to the crew and the saving of the machinery, not having mud or oil thrown over the machinery, and in the fire hazard feature.

Q. What is the average cost, labor and material for one of these wire line wipers?

A. The average was $5.00 last year.

Q. And what was the average retail selling price? A. $12.10.

Q. Are there competing devices?

A. There are a few devices, but most of those are quite unsatisfactory. This device, I think, is by far the most satisfactory on the market. It is much cheaper to operate, and simpler, and safer.

Q. Have all molding and die casts and development been completed on this? A. Yes, sir.

Q. Could you illustrate just shortly how one of those [242] wire line wipers operates, just very briefly?

A. This is pulled open to wind on the wire. When it is on the wire it grips it with a very heavy grip, just like a winding tower on a rig. And it has got the resilience of the rubber itself. It has no holes through the center, and yet the wire rope goes through the center. The molding is such that it has a very heavy grip, and as the rope goes on through it wipes the mud or oil off beneath. It is very simple. The same principle applies on the other one, except the other one has a replaceable rubber, has

(Testimony of J. C. Ballagh.)

an adjustment, so that the rubber can be tightened up. The rubber on this steel housing—steel lasts much longer, and the refill rubber itself costs less, and it has a spring actuated release. So when the bailer or core barrel comes to the surface it is disengaged automatically.

Q. What is the purpose and function of the steel clad protector?

A. The function of the steel clad protector is to stabilize the drilling in the open hole beneath the casing and to protect the tool joints themselves from wear. In drilling an oil well a certain length of casing is set, and beneath that the bit operates in the open hole, and if the formation is abrasive the tool joints wear very rapidly.

Q. I believe an application for patent has been filed on that? A. Yes, sir. [243]

Q. And some claims have been allowed?

A. Yes, sir.

Q. And has that been assigned by Mr. Miller to the corporation? A. Yes, sir.

Q. What is the average manufacturing cost on the open hole tool joint protector?

A. I think about $8.00.

Q. What is the average retail price?

A. About $25.00.

Q. Is there any competing device?

A. Not at the present time.

Q. Are sales of the open hole tool protector being pushed at the present time? A. No. sir.

Q. Why is that?

(Testimony of J. C. Ballagh.)

A. On account of the priority on the steel, steel castings, welding rods and pipe, all of which are almost impossible to get on the priority that has been assigned to the oil industry.

The Court: We will take a few minutes recess at this time.

(Short recess)

Q. By Mr. Bednar: Mr. Ballagh, about how many protectors has your company sold in its history?

A. Somewhere between 750,000 and 900,000.

[244]

Q. I believe you testified the other day that of all the protectors in use in the world approximately 75 percent were being sold by your company?

A. Yes, sir; that is my best estimate.

Q. Approximately, and on the average, how many protectors did your company sell each year, 1939, 1940, and 1941?

A. About 30,000 per year.

Q. Referring you to Defendants' Exhibit B, does this chart indicate that in 1939 approximately 20 percent of all protectors sold in California were put on by the hydraulic applicator?

A. About 20 percent of those sold by Patterson-Ballagh.

Q. And that is in California? A. Yes, sir.

Q. And is it also correct, according to this chart, that in the Mid-Continent area, in 1939, approximately 25 percent of all protectors sold by you in that area were put on by the hydraulic applicator?

(Testimony of J. C. Ballagh.)

A. Yes, sir.

Q. And in 1940 are the percentages indicated on the chart correct? A. Yes, sir.

Q. In other words, of the California volume of protectors sold by your company in 1940, 75 percent were put on by hydraulic applicators?

A. Yes, sir. [245]

Q. And in the Mid-Continent area 25 percent were put on by the—— A. Yes, sir.

Q. And in 1941, is it correct that in California 95 percent of all protectors sold by you were put on by the hydraulic applicators? A. Yes, sir.

Q. And 35 percent in the Mid-Continent area?

A. Yes, sir.

Q. That is the hydraulic applicator of defendant? A. Yes, sir.

Q. Which is the subject of your agreement with the Bettis Rubber Company?

A. Yes, sir; the cross agreement.

Q. You have never paid any royalty to the Bettis Rubber Company under that agreement?

A. No, sir.

Q. And the hydraulic applicator, plus the transfer sleeve that you use—the hydraulic applicator, that is royalty free under the Bettis Rubber Company agreement? A. Yes, sir.

Q. What has been the reaction of the trade, if you know, to the steel clad tool joint protector of Mr. Miller?

A. It has been very favorable in areas where the formation is abrasive.

(Testimony of J. C. Ballagh.)

Q. Can you give us an example of such area? [246]

A. Castiac, California, and several fields in Wyoming, and several fields in Arkansas, and Northern Louisiana and West Texas.

Q. I note here Defendants' Exhibit A, steel clad protectors $597.29. When you refer to these areas, are you referring to areas where these protectors have been sold since 1939 or prior?

A. In a number of these areas we haven't sold them. We put them out on trial for the customers, and we wouldn't bill them. In many of the cases it was for our own information. We would bill the steal clads up in Castiac, and sometimes in Avenal, California.

Q. Referring to Mr. Miller's sucker rod protector, rod style, will you explain the purpose and function of that, and wherein it differs from the box style?

A. In the box style protector, the box is fitted on the end of the rod, and the box and the rod together move up and down, and the plastic protector contacts the inside of the tubing, and there is a direct wearing action between the two against the inside of the tubing. In the box style protector, the protector is molded directly onto the rod, and the protector will lay against the side of the tubing, and the rod will move down inside the protector, and it forms a smooth bearing between the tubing and the rod, so that the oil lubricates it, so that any wear that takes place is against the plastic, which is fairly soft, and

(Testimony of J. C. Ballagh.)

against the [247] smooth rod itself, whereas with the box style the friction is against the rough tubing.

Q. Is the rod style protector slowly replacing the box style protector?

A. In my opinion, it will eventually entirely replace it, where there are difficult pumping conditions.

Q. Has an application for patent been filed by Mr. Miller on the rod style?

A. Yes.

Q. And that was just recently, was it not?

A. Yes, sir.

Q. What is the approximate cost of labor and material of the rod style sucker rod protector?

A. I haven't got the—I think it is approximately $2.00, cost of labor and material.

Q. What is the average retail price?

A. I think it is about $6.50. I would like to check that, if you want it exactly, but I think that it is approximately what the selling price is.

Q. Is there any competition on the rod style sucker rod protector other than the box style?

A. As far as I know, there is no design like that. There are many wearing devices used on sucker rods, but none of them have the inside wearing surface; they are all outside wearing surfaces.

Q. Is the sale of the rod style protector being pushed [248] at the present time?

A. It is being pushed in connection with the manufacture of the rods themselves. We haven't been able to buy many of the rods, but the companies that

(Testimony of J. C. Ballagh.)

make the sucker rods themselves have been working with us, and we have been selling to them.

Q. What has been the reaction of the trade to the rod style sucker rod?

A. It has been very favorable, extremely so. I think its future is very, very bright.

Q. Now, who invented the sucker rod wiper?

A. Mr. Miller.

Q. Will you explain the nature and function of the sucker rod wiper, and how it works?

A. A sucker rod wiper is a steel housing, in which there are two rubber discs, and the rubber discs wipe the sucker rod that goes through in the same manner that the pipe is wiped in the pipe wiper. There is a floating rubber disc with a hole in the center through which the sucker rods are thrust, and as the sucker rods are pulled from the well the oil is wiped from the rods. At the top is a safety device so that when the rods drop they will be automatically caught, and not fall back into the well.

Mr. Bednar: I offer in evidence a picture of the sucker rod wiper of Mr. Miller.

The Clerk: Defendants' Exhibit O. [249]

Q. By Mr. Bednar: Do you know whether there has been an application for patent filed on this yet?

A. I don't think it has got beyond the affidivit stage. It may have been filed. I am not positive about it.

Q. What is the cost of material and labor in the manufacture of that device?

A. $16.10.

(Testimony of J. C. Ballagh.)

Q. And what is the average retail price?

A. $48.00.

Q. Are there any competing devices?

A. Yes, there are a number.

Q. What has been the reaction of the trade to this device?

A. It has been very favorable. It overcomes several of the objections. I think, however, the market is somewhat limited, as it does not wipe under pressure. There are hundreds of thousands of wells that have no pressure, so it has quite a wide market, but is not in universal use.

Q. Are the sales of that device being pushed at the present time? A. No.

Q. That is on account of steel priorities?

A. On account of steel priorities.

Q. Have your molds been made, etc.?

A. Yes, the molds and all the patterns have been made, and the jigs necessary. [250]

Mr. Bednar: That is all.

Cross Examination

By Mr. Lamont:

Q. Mr. Ballagh, of course you are familiar with the three raises in salary that you were given during the years of 1939 and 1940, are you not?

A. Yes, sir.

Q. Mr. Miller voted in favor of all those raises, did he not?

A. I believe so, except those for himself.

Q. And you voted in favor of those for him, did you not? A. Yes, sir.

(Testimony of J. C. Ballagh.)

Q. During this period did Mr. Armington ever vote contrary at any meeting to you or Mr. Miller?

A. I don't believe so. The minutes will speak for themselves.

Q. But you don't recall that he ever did?

A. No.

Q. You have spoken several times during your testimony of non-protector itmes? A. Yes, sir.

Q. Included in that term were items, were there not, upon which you paid royalties to other people?

A. Yes, sir.

Q. Will you, referring to this chart, just state what [251] those items were and the amount of royalties that you paid?

A. In 1939——

Q. In 1939—take that.

A. In 1939 we paid $750.12 on the wire line guide.

Q. What were your gross sales on that item?

A. They were $33,522.18. That, however, included the refill rubbers, on which we pay no royalty, and it includes the steel parts, steel wire and steel castings used in connection therewith, and on which we pay no royalty. We pay royalty only on the refill rubbers themselves used in the initial devices sold.

Q. Would there be any possibility of breaking down that item? A. Yes.

Q. As to gross sales?

A. We pay a 10 percent royalty, which would mean on the devices under which royalty was paid, $7501.20.

(Testimony of J. C. Ballagh.)

Q. Will you take the same item and give your testimony as to 1940?

A. In 1940 the wire line guide royalty was $458.82. The gross sale of the guides and refills, the metal parts in connection therewith, was $32,694.98.

Q. How much of that item was royalty paid on?

A. On $4588.20.

Q. Will you state the same facts as to 1941?

A. The royalty was $412.38, with gross sales of [252] $34,996.84. The sales of the items covered by the royalty were $4,123.80.

Q. What is the next item, and state how much you paid in royalty, and in 1939 what were the gross sales?

A. The gross sales were $11,633.33. The royalty paid was $1,770.22.

Q. Give the same information as to 1940.

A. The gross sales were $7797.61. The royalty was $858.77.

Q. Take the next item upon which you paid royalty.

A. Do you want 1941 for that payment?

Q. Yes.

A. 1941 was $6,111.43, with a royalty of $665.32.

Q. Now will you give us the next item upon which you paid royalty?

A. The next item is mud guns.

Q. What was the gross for 1939, the gross sales?

A. The gross sales were $574.87 on one device on which we paid a royalty, and $5983.51, upon which we

(Testimony of J. C. Ballagh.)

paid no royalty. And the royalty was $45.99 on the $574.87 amount.

Q. Will you give the same information as to 1940?

A. In 1940 the sales on which we paid royalties were $2853.25, on which we paid a royalty of $228.26.

Q. What was the next? How about 1941?

A. In 1941 we have a gross sale of $5287.95, and there was no royalty. [253]

Q. Now, what is the next item upon which you paid royalty?

A. In 1940 there was a sucker rod wiper, the sales of which were $389.50, on which we paid a royalty of $38.95. In 1941 the sucker rod wiper sales were $384.30, on which a royalty of $38.42 was paid.

Q. Any other items?

A. As far as I know, that is the total.

Q. I believe you testified that prior to the formation of the partnership with Mr. Miller you were employed by the Pomona Pump Company?

A. I had no partnership with Mr. Miller.

Q. I don't mean with Mr. Miller. I mean with Mr. Patterson. A. Yes, sir.

Q. How much were you paid by that organization?

A. I was on a commission basis. I think I grossed about $700 or $800 a month.

Q. And after that you were employed by the Johnston Pump Company, were you not?

A. You said at Pomona?

Q. Yes.

(Testimony of J. C. Ballagh.)

A. With Pomona, I think I was making about $500 a month with the Pomona.

Q. And with the Johnston about $800?

A. I think that was about between $700 and $800.

[254]

Q. Mr. Ballagh, I want to ask you whether, at the time of the taking of your deposition in this matter, which was on June 23, 1942, you did not testify as follows, page 52:

"Q. Can you give an estimate, even though a rough estimate, as to the percentage of profits accruing from the sale of protectors and stabilizers?

"A. Not with any degree of exactness, because we kept no basis of cost on the individual commodities. We had practically the same method of calculating our costs, and all the items we sold had approximately the same mark-up, and any gross margin was applicable to gross profits. Against the gross profits will accrue the overhead and sales and other expenses, so we end up the year with some sort of a net profit; but how that net profit would be per item, I could not say. Is that close enough for what you want?

Q. Would it have any relation to the percentage of gross sales of the different articles?

"A. Yes, I would say very materially.

"Q. In other words, it would trot along pretty well with the percentage of gross sales?

"A. Fairly so, except that during certain periods we may have excessive amounts of costs that would be thrown into the expense, in the way of die costs

(Testimony of J. C. Ballagh.)

and patterns and amortization of experiments that we might be making.

"Q. But other than that, generally speaking they would go hand in hand; is that correct? [255]

"A. Well, I don't believe I could make any rule that would give it. I would say, as we increased our sale of casing protectors, our profit would very probably go up to the percentage of sales accruing to casing protectors."

You testified in the manner that I have read, did you not?

A. Yes, substantially that way.

Q. Before you perfected your hydraulic applicator there were other hydraulic applicators on the market, were there not?

A. Yes, but not with a transfer sleeve.

Q. But other than that, there were such applicators?

A. Yes, but not with the transfer sleeves.

Q. But this applicator was developed by you, was it not, to handle that particular thing?

A. Yes, sir.

Q. Was there a pipe wiper on the market before you put yours on?

A. Not that I ever heard of.

Q. Haven't you received a notice of infringement from the Shell Oil Company in regard to that?

A. Yes, sir.

Q. And the question as to the infringement remains at this time undetermined?

(Testimony of J. C. Ballagh.)

A. That notice was received prior to the issuance of our patent, I think about a year. [256]

Q. But there has been no determination?

A. As far as I know, nothing was done about it.

Mr. Lamont: If the Court please, I have some more questions of this witness, but I think it will speed things up very decidedly if we could have a recess now until 2:00 o'clock.

The Court: Very well.

Mr. Lamont: I will have my matter in shape, and I think we can make time.

The Court: Very well. We will suspend until 2:00 o'clock.

(A recess was taken until 2:00 p. m. of this same day.)

Afternoon Session—2:00 o'Clock.

Mr. Lamont: If agreeable to the Court, I would like to put on two witnesses out of order, so that they may leave.

The Court: Very well.

Mr. Lamont: Mr. Grant, will you take the stand?

JOHN M. GRANT,

called as a witness on behalf of plaintiff, being first duly sworn, testified as follows:

The Clerk: Will you state your full name?

The Witness: John M. Grant.

(Testimony of John M. Grant.)

Direct Examination

By Mr. Lamont:

Q. Mr. Grant, where do you reside?

A. South Pasadena, 1221 Marengo Avenue.

Q. What is your occupation?

A. Purchasing agent.

Q. For what company?

A. Bell and Loffland, Inc.

Q. How long have you been such?

A. I have been with this company eight years.

Q. What is the nature of that company's business?

A. Oil well drilling contractors.

Q. How do they compare in size with other companies? [258]

A. They, with their associate company, Loffland Brothers, I believe are the largest firm of oil well drilling contractors in the world.

Q. Have you had any occasion to purchase protectors of different types? A. Yes.

Q. What types of protectors have you purchased?

A. Well, I have probably purchased from time to time practically every type that has been made.

Q. Among those protectors, you have purchased protectors from Patterson-Ballagh, have you?

A. Yes, sir.

Q. Looking at these two protectors, Mr. Grant, are you familiar with both of those types of Patterson-Ballagh protectors?

A. In a general way, yes.

(Testimony of John M. Grant.)

Q. One, I believe, is the protector without lips, and the other is the protector with lips?

A. That is right.

Q. That is true, is it not?

A. Yes, sir.

Q. Your company has had occasion to use those protectors, has it, of that type?

A. Yes, at times.

Q. Apparently the one with lips is very similar to the other form of protector, except that it has been streamlined, [259] has it?

Mr. Bednar: We object to that, if your Honor please.

The Court: I think so.

Q. By Mr. Lamont: Your company has used those types? A. Yes, sir.

Q. To what extent is there an advantage in having lips on a protector over the other type?

Mr. Bednar: May I ask a question on voir dire, your Honor?

The Court: Yes.

Q. By Mr. Bednar: Mr. Grant, have you ever seen these in operation in the field?

A. I have seen them on pipe. You can't see them in operation. They are down in the well.

Q. When they have been out of the hole, have you seen them?

A. Yes, sir.

Mr. Lamont: Now will you read my question, please?

(Question read by the reporter.)

(Testimony of John M. Grant.)

A. I don't know that there is any.

Q. By Mr. Lamont: Does it make it stick any firmer to the drill pipe or not?

A. Well, in my opinion it does not.

Q. As a matter of fact, the firmness with which it adheres to the drill pipe depends upon the length of the protector, does it not?

A. I would say so.

Q. And a protector without lips, of the same length, would have the same clinging power, would it not?

A. The only addition of the lipping arrangement that you could possibly work up here would be the length of these lips and that shouldn't amount to an awful lot in the overall length and tensile strength in the balance of the protector.

Q. According to the testimony heretofore given in this case, sometimes a protector would cause a groove on the drill pipe. Are you familiar with that?

A. I have heard that discussed, yes, and I have probably seen one or two cases of it.

Q. Is that ever of any serious consequence?

A. I would say not. In comparison to the general wear and tear on drill pipe, it is not a particular item.

Q. Occasionelly these protectors have been known to slip. Are you familiar with that?

A. Well, I believe they do, yes.

Q. Is that of any serious consequence when it occurs? A. No, not to the operator.

(Testimony of John M. Grant.)

Q. Do you know what a hydraulic applicator is?

A. Yes, sir.

Q. With what variety of such an applicator have you been familiar?

A. I have seen the one used by the Bettis people, and I have seen the one used by E. M. Smith. I have not only [261] seen them, but I have seen them in operation.

Q. As far as you know, what hydraulic applicator was first on the market?

A. The first one I knew of was the one Bettis had.

Q. Do you know the first use of that patented device?

A. I couldn't say the first use, except that I know that when I first saw it it was on a pipe on a well we were drilling for an oil company in the Cole's Levee district.

Q. Referring to this Bettis applicator, with what speed is it possible to install a protector?

A. Well, the applicator and the two men which are furnished to work the machine and install the rubbers on the pipe, they were fast enough that it didn't keep the others waiting like they were waiting for the crew at times.

Q. Have you ever had any conversations with Mr. Ballagh as to the Patterson-Ballagh applicator?

A. No, sir, I don't believe I have.

Q. Are you familiar with pipe wipers?

A. I have seen those in operation.

(Testimony of John M. Grant.)

Q. What makes?

A. I have seen both the Bettis and the Ballagh.

Q. In your opinion, did the Bettis pipe wiper have any superiority—or did the Ballagh pipe wiper have any superiority over the Bettis wiper?

A. No, sir.

Q. Which one of those two did you see first?

[262]

A. Now, that I wouldn't be able to say for sure, but I will say that, as far as I can remember, the first person that I met out of the Los Angeles office was for the Bettis Pipe Wiper. It may have been that in some emergency sometime in the field, that this pipe had been ordered previous to that, but I don't recall.

Q. Where are protectors usually placed on the drill pipe?

A. As far as we are concerned, we like to have them as close under the tool joint box as possible, and not so close that they will interfere with the elevators.

Q. What make of protector has your company been in the habit of buying?

A. We have been using the Bettis for several years.

Q. Have you had any trouble with protectors slipping?

A. Not recently. Years ago we used to have trouble with protectors slipping on the pipe, but nothing in the last several years.

Q. What was the cause of the slipping?

(Testimony of John M. Grant.)

A. Well, there may have been two or three things that caused it. One was, I believe, that they didn't make the protectors long enough for the job they were supposed to do, and I think the quality of the rubber material had considerable to do with it.

Mr. Lamont: That is all then. [263]

Cross Examination

By Mr. Bednar:

Q. Mr. Grant, have you ever used a lip protector? A. Yes, sir.

Q. Where has your company done most of its drilling?

A. I believe we have drilled in every field in California, with possibly one or two exceptions.

Q. Have you done much, if any, drilling in the last three years outside of California?

A. We never drill out of the State.

Q. Then your opinion on the lip protector is based on your experience in California?

A. Yes, sir.

Q. Have you used the lip protector in any quantity? A. No great quantity, no.

Q. Have you used enough of them to know what percentage of the two types of protectors tear on being applied to the drill pipe, which one tears easiest in applying them to the drill pipe?

A. No, I wouldn't know anything about that, because we are not concerned with that.

Q. I just wondered if you had observed it. I

(Testimony of John M. Grant.)

realize the manufacturer pays for the torn protectors.

A. I have seen quite a few protectors put on pipe, and I never saw one tear; I will put it that way — probably a coupe of thousand or maybe three thousand. [264]

Q. This hydraulic applicator that you mentioned seeing, which seemed to put the protectors on fast enough, where was it in operation?

A. It was on a well in the Cole's Levee field.

Q. Was it in the derrick, or where?

A. The applicator was on the ground. The device itself was right by the derrick.

Q. Was there a transfer sleeve being used?

A. Yes, sir.

Q. Have you ever witnessed any tests as to which hydraulic applicator is the fastest? A. No.

Q. This time when you testified that you saw the hydraulic applicator working right alongside the well, were the rings installed up in the derrick?

A. Yes; yes, they were installed as the pipe was going in the hole.

Q. In other words, they weren't being installed on the pipe away from the derrick?

A. No, not in that case.

Q. What experience have you had in drilling in the Mid-Continent, if any?

A. The company I am with doesn't drill there, as I said. I have been in the Mid-Continent. I have never worked for an oil company in the Mid-Continent, but I worked for a supply company there. [265]

(Testimony of John M. Grant.)

Q. Do you know whether they have more trouble with ringing the pipe in the Mid-Continent than they have in California?

A. What do you mean "ringing the pipe"?

Q. By reason of the protectors rotating on the pipe and wearing it away?

A. I wouldn't know about that. I haven't ever seen any data on it, and I don't know of any such trouble that they may have had.

Mr. Bednar: That is all.

Mr. Lamont: That is all. Mr. Wiese. [266]

WALTER H. WIESE,

called as a witness in behalf of plaintiff, being first duly sworn, testified as follows:

The Clerk: State your full name.

The Witness: Walter H. Wiese.

Direct Examination

By Mr. Lamont:

Q. Mr. Wiese, where do you reside?

A. San Marino.

Q. What is your occupation?

A. Secretary and treasurer of Byron Jackson Company.

Q. As a part of your duties, do you have supervision of the accounts of that company?

A. I do.

Q. Will you turn to the account of that com-

(Testimony of Walter H. Wiese.)

pany showing the investment of Byron Jackson in Patterson-Ballagh, and will you state to the Court what that account shows?

Mr. Bednar: Just a minute. Can I ask one question. Mr. Wiese, aren't your accounts based on what certain items cost you?

A. They are based upon the facts as recorded.

Q. For instance, does it show the Hopkins patent down there? A. The Hopkins patent?

Q. Yes. [267]

A. Well, is your question the cost of the Hopkins patent? Is that what you want to determine? Is that what you are asking me?

Q. I am asking you this. You are trying to get at the investment of Byron Jackson in the defendant?

Mr. Lamont: Yes.

Mr. Bednar: And the record so far shows that $25,000 was paid for 250 shares of stock.

Mr. Lamont: And I want to show, in addition, that $75,000 was expended by the Byron Jackson Company, as to which an exclusive license was given to Patterson-Ballagh.

Mr. Bednar: I don't believe the cost of the Hopkins patent at all concerns us.

The Court: It probably wouldn't, if you hadn't tried to show the amount of investment of the company.

Mr. Lamont: That is the point. I want to forestall an argument based on that $25,000 which you put in evidence.

(Testimony of Walter H. Wiese.)

Mr. Bednar: I will put it in providing you put in a copy of the Hopkins patent and show what it is.

Mr. Lamont: Have you got a copy of the Hopkins patent? I have no objection to that.

Mr. Bednar: In other words, as I see it, we are bordering on the question of whether or not these four agreements are one or not one, and determining the amount of the investment.

Mr. Lamont: They argued that a considerable length [268] in the other case, the question of the amount of investment. I will offer this Hopkins patent in evidence.

The Clerk: Plaintiff's Exhibit 20.

Q. By Mr. Lamont: Now, Mr. Wiese, what do the books of the company show as to the amount of investment in Patterson-Ballagh?

A. The account here shows payment on September 20, 1928, of $12,500.00 to C. L. Patterson and $12,500 to J. C. Ballagh, and an additional cost of $75,000 for the Hopkins patent.

Mr. Lamont: That is all. Take the witness.

Cross Examination

By Mr. Bednar:

Q. Was the cost of the Hopkins patent ever communicated to Patterson-Ballagh, do you know? Was it taken into consideration by Patterson-Ballagh, if you know?

A. That is a matter of their records, isn't it?

Q. Were you with the company in 1928?

A. Not in 1928, no.

Mr. Bednar: That is all.

Mr. Lamont: That is all. [269]

J. C. BALLAGH, recalled

Cross Examination, resumed

Mr. Bednar: I might bring to the Court's attention at this time that the license of the Hopkins patent has to do only with the rubber part, a pipe with a groove in it, and——

The Court: I am not interested in that, am I? You introduced a table showing an investment of $25,000.00, and a return on that investment of several hundred thousand dollars.

Mr. Bednar: I am showing that they retained the metail parts, but we never did get the patent on the metal parts.

Mr. Lamont: You got it, and then licensed it back.

Mr. Bednar: No.

Mr. Lamont: That is what the contracts show that are in evidence.

Mr. Bednar: You had the right to——

The Court: I think I should have sustained an objection to that statement in the first place, showing that investment.

Mr. Lamont: I probably should have made it, but it came in as a part of an exhibit.

The Court: Yes.

Mr. Lamont: I agree with the Court. I don't think there is any materiality at all in the question of the amount of investment here.

Q. By Mr. Lamont: Mr. Ballagh, the inventions of Mr. [270] Miller, as to the amount of gross sales, are represented, are they not, by these yellow——

(Testimony of J. C. Ballagh.)

A. Yes, sir, yes, sir.

Q. I don't know what you would call them.

A. Areas.

Q. Areas on this exhibit. I now refer to Exhibit A. That is correct, is it not? A. Yes, sir.

Q. In other words, they are very inconsiderable in amount as to the total of those sales during those years?

A. They amount to about $6000, and I don't consider that inconsiderable.

Q. $6000 out of $366,000—that is correct, is it not? A. That is correct, yes, sir.

Q. Now coming to the pipe wipers, what do they represent out of the total gross sales?

A. In 1941 they were $43,862.60.

Q. Out of a gross of over $366,000?

A. Yes, sir.

Q. How about 1940?

A. They were $30,189.50.

Q. Out of a gross of $329,000?

A. Yes, sir.

Q. And how about 1939? A. $12,296.00.

Q. Out of a gross of over $336,000; that is correct, [271] isn't it? A. That is correct.

Q. Looking at your tubing protectors, in 1939 what do they they represent? A. $3294.00.

Q. Out of a gross of over $336,000?

A. That is correct.

Q. How about 1940? A. $8527.20.

Q. Out of a gross of over $329,000?

A. That is correct.

(Testimony of J. C. Ballagh.)

Q. How about 1941? A. $16,691.40.

Q. Out of a gross of over $366,000?

A. That is correct.

Q. And the other patented articles of your invention and Mr. Miller's invention were even smaller in amount of sales? A. Yes, sir.

Q. Your manufacturing plant is still in Los Angeles, is it not? A. Yes, sir.

Q. How large a plant is it, the dimensions of it?

A. We cover about a third of a block, in which the plant is located, part of it one floor and part two floors. Across the street we have approximately one-third of that [272] block, on which is located our warehouse.

Q. Blocks vary in area. Can you give us some idea in feet?

A. I don't remember the square feet. I can get it from Mr. Miller, if you would like to get it. I think he remembers what it is.

Mr. Bednar: I will supply the square footage.

Mr. Lamont: Can we get it now?

Mr. Bednar: Yes. According to Mr. Miller, of the factory, one floor is 120x125 feet, and the second floor is 120x60, and the warehouse is 240x30.

Q. By Mr. Lamont: The dimensions he has given me include everything, do they not?

A. They include warehouse and office and everything else in that locality.

Mr. Bednar: That is right.

Q. By Mr. Lamont: How many employees did

(Testimony of J. C. Ballagh.)

you have at this plant you have just referred to during the years 1939, 1940 and 1941?

Mr. Bednar: That has already been gone into before.

Mr. Lamont: It was gone into in the depositions, not as to this particular plant; it was all told, over all. A. About 25, I think.

Q. That includes everybody, stenographers and everybody else, does it? A. Just about. [273]

Q. Now, your establishment in Texas, at Houston—— A. Yes, sir.

Q. That is a demonstration and assembly establishment, is it not?

A. Partly that. It is our headquarters for our Mid-Continent operation.

Q. Do you do any manufacturing there?

A. We service our installation tools and assemble our mud guns, assemble some of the swivel bumpers, and assemble various devices, and any alterations to be made that can be made without any machine work. We install our tubing protectors there, and we have a hydraulic press and a drill press. We have electric drills and grinders, and do what repair work is necessary.

Q. Strictly speaking, there is no manufacturing there, is there? A. Not as such, no.

Q. Your other offices, do they amount to any more than sales offices?

A. At New Iberia, Louisiana, we have our own little buildings, in which we have our sales and warehouse combined.

(Testimony of J. C. Ballagh.)

Q. How many employees there?

A. Two, sometimes three.

Q. How about Houston, how many employees?

A. In Houston we generally have four that work directly out of Houston. [274]

Q. Now as to the other offices, what do they amount to?

A. They are service stations, where we keep our installation tools and hydraulic equipment, and where we keep our branch stock.

Q. How many of those are there?

A. We have one at Victoria, Texas, one in Shreveport, Louisiana, one at Ventura, and one at Avenal, one at Casper, and one at Turner Valley, Canada, and we have service, but without hydraulic machines, in Odessa, West Texas, and at Fairfield, Illinois and Oklahoma City; and I think I omitted Bakersfield.

Q. Is that all? A. As well as Los Angeles.

Q. Have you another location in Los Angeles?

A. Yes. We service out of the factory for the Southern California area.

Q. And is that any different location than the factory location?

A. No; it is at the factory.

Q. Now, as to other offices, how many employees do you employ all told, in all of them together?

A. Our total employees directly on our payroll run, I think—I think during 1941 they were about 43, I think they were, an average. They have run during that period from 35, I think, up to 43.

Q. Mr. Ballagh, in 1938 the minutes show that

(Testimony of J. C. Ballagh.)

you have at this plant you have just referred to during the years 1939, 1940 and 1941?

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Q. Mr. Ballagh, in 1938 the minutes show that

(Testimony of J. C. Ballagh.)

your [275] salary, in October, 1938, was increased; that is correct, it it not?

A. I can't remember. If the minutes show it, it is a fact.

Q. Your salary was increased in 1938, you recall that, don't you? A. I can't recall 1938.

Mr. Lamont: That is a fact, isn't it?

Mr. Bednar: Yes.

Q. By Mr. Lamont: What I want to ask you is this: That was with the understanding, was it not, that if the profits didn't bear up, your compensation would be decreased?

A. I don't remember that.

Q. As a matter of fact, your salary later on was decreased, wasn't it, from $1500 to $1000; that is correct, isn't it?

A. If the minutes show it, if the record show it, it is a fact.

Q. Since Mr. Miller came into the business have there ever been and decreases in salaries?

A. No, not that I know of.

Q. Before Mr. Miller came into the business, and while Mr. Patterson was there, at least, he was going into inventions and matters of that type, was he not? A. Mr. Patterson?

Q. Yes. In other words, your company——

[276]

A. I knew of none that he went into for the corporation.

Q. Wasn't your company dealing with such things at that time?

(Testimony of J. C. Ballagh.)

A. Outsiders—we had at that time the license on our wire line guide and on our swivel bumper and our mud gun.

Q. Didn't your company make some investigation into matters of that type?

A. We have made investigation at various times.

Q. And you did while Mr. Patterson was with the company? A. Yes, sir.

Q. And reports were made to the Board of Directors with regard to those matters, were they not?

A. I think they were.

Q. Since Mr. Miller came into the business, has there ever been any report made to the Board of Directors as to any inventions or examinations of inventions of other people, or anything of that kind?

A. I don't remember a directors meeting that we had at which we didn't tell Mr. Dulin and explain various devices we were working on. I can't recall any specific conversation.

Q. Can you recall that you ever did at any meeting of the directors?

A. Yes, I can recall that we have.

Mr. Lamont: Mr. Bednar, you will stipulate that the minutes don't show any such report? [277]

Mr. Bednar: I am not sure whether they do or not, Mr. Lamont.

Mr. Lamont: It is very clear in referring to the A-66 minutes that the reports were there made apparently as to experimental work connected with the business.

(Testimony of J. C. Ballagh.)

The Witness: While Mr. Patterson was with the business?

Q. By Mr. Lamont: Have you or Mr. Miller, during this period of 1939, 1940 and 1941, ever effected any improvements or inventions which you have obtained which have not been assigned to the company? A. None of mine.

Q. How about his?

A. I don't know of any of his that have not been.

Q. Are you making both types of protectors at the present time? A. Yes, sir.

Q. Do the two protectors vary in price?

A. No; they are identical.

Q. Coming to pipe wipers, you gave some testimony as to the percentage of total business of pipe wipers done by Patterson-Ballagh. How many wells were equipped with pipe wipers during the years 1939, 1940 and 1941?

A. I can't tell the number of wells, because in some cases there would be three or four on one well, and in other cases they would last for ten or twelve wells. I have no [278] way of knowing how many wells we have equipped.

Q. Or the percentage of wells equipped with your pipe wipers?

A. No. I will say that the majority of deep wells and wells of any size drilled by major oil companies were buying supplies—major drilling contractors, had the pipe wipers on.

(Testimony of J. C. Ballagh.)

Q. The majority of them had yours, you mean?

A. The majority of them, yes, sir.

Q. How many pipe wipers did you sell in those years, that is, the dollar value, but not the number?

A. They averaged $31 during that period, and you can divide one by the other, and it will give you the approximate number.

Q. What percentage of wells were equipped with wire line guides of your manufacture?

A. In what area, and during what year?

Q. Well, for all oil wells during the years 1939, 1940 and 1941.

A. We didn't manufacture them, I don't think, during the year 1939. I think they were just started in 1940, and then were sold in 1941.

Q. 1940 and 1941?

A. I would say, taking all wells as a whole, just a very few percent. A great number of wells never used any wire rope at all in the well. [279]

Q. You said that you were having difficulty in securing steel to manufacture certain products?

A. Yes, sir.

Q. How long has that condition existed?

A. Oh, it has been getting constantly more acute for the past year. Our biggest trouble in the last year has been getting the little accessories that go with it. For instance, welding rods it has been almost impossible to get without a rating higher than we have, and without welding rods we couldn't do very much fabrication.

(Testimony of J. C. Ballagh.)

Q. In making these inventions it was necessary to have certain materials, was it?

A. Yes, sir.

Q. Who paid for those materials—you or Mr. Miller or the company?

A. The Company.

Q. You testified that you were manufacturing bakelite. That was a secret process?

A. Yes, sir.

Q. Who was the first one to start working on the secret process—you or Mr. Miller or Mr. Patterson?

A. Mr. Miller. Mr. Patterson worked some on the process. Mr. Patterson hasn't made any of this new composition at all.

Q. Also in your testimony you stated your retail prices on these different gadgets of your invention and Mr. Miller's [280] invention?

A. Yes, sir.

Q. Let me ask you, what was the extent of the discount on those retail prices? What did you actually net on those?

A. The prices I gave you were the prices the customer paid. We had a 2 percent cash discount, and if he bought them direct he paid that price, less the 2 percent cash discount. If he bought them through a supply store the supply store had a 10 percent discount. And if he bought them through one of our agents who sold the supply store, and then was given some service, we sold our agents generally at about a 25 percent discount. But the

(Testimony of J. C. Ballagh.)

price the customer paid was what is shown on our discount sheet, less 2 percent for cash.

Q. Out of that retail figure would also come overhead, would it not, and also sales expense?

A. That was the gross dollars that we received at the factory, and from it was paid all of our costs.

Q. Who was the first inventor of hydraulic applicators, do you know?

A. I think a man by the name of Minor.

Q. Didn't you at one time concede priority of invention to Bettis?

A. No. There was an interference, at which certain of his claims interfered with certain claims of ours, and we may a cross license, under which he took those that had to [281] do with our device, and we took those that had to do with his.

Q. You received from Bettis, apparently, a license?

A. Yes, sir. We had a cross license. We licensed them and they licensed us.

Q. Have any claims ever been allowed on your application for patent covering your lip protector?

A. No, sir, not yet.

Q. Referring to your plastic tubing protector and the plastic sucker rod protector, what percentage of wells employ protectors?

A. Of all wells?

Q. Yes.

A. That is pretty hard to say. There are about

(Testimony of J. C. Ballagh.)

800,000 or 900,000 wells in the United States, and I think we have probably got them on possibly a thousand wells.

Q. In other words, the percentage, in any event, is very small, the total?

A. Yes, sir; they are used only in areas where there is extreme deep pumping, and where this pulsation occurs that occurs in certain fields in certain areas. In the shallow wells that trouble does not take place.

Q. There is a very limited market for that sort of thing?

A. I would estimate that there is probably another hundred thousand wells that they could be applied to, and probably there are new wells being put on production constant- [282] ly enough to insure probably a constant, steady market.

Mr. Lamont: I think that is all.

Redirect Examination

By Mr. Bednar:

Q. Mr. Ballagh, Patterson-Ballagh Corporation doesn't pay any royalties at all to yourself or Mr. Miller for anything you have invented during the time mentioned in this trial? A. No, sir.

Q. How long ago did you get this notice of infringement from the Shell Oil Company?

A. I think it was about a year before the patent issued.

Q. Following that notice did your patent attorneys write the Shell Oil Company a letter?

(Testimony of J. C. Ballagh.)

A. Yes. They explained the construction of our device.

Q. Have you heard from the Shell Oil Company since then?

A. As far as I know, Shell has never answered that letter.

Q. From your experience in the field, does the hazard of ringing the drill pipe by reason of the old style protector occur more frequently in California or in the Mid-Continent?

A. It is very uncommon in California. I have only [283] seen two instances since I have been in business in California, and it was of minor consequence. It was almost entirely in the Mid-Continent area, due to the difference in the mud velocity; they carry very much higher mud velocities, and the drilling is different. They are drilling through softer formations, and they require higher pressures, and much faster drilling.

Mr. Bednar: That is all.

Mr. Lamont: That will be all. Mr. Chesnut, will you take the stand? [284]

JOHN CHESNUT,

a witness heretofore duly sworn, upon being recalled, testified as follows:

Direct Examination

By Mr. Lamont:

Q. Mr. Chesnut, where do you reside?

(Testimony of John Chesnut.)

A. La Canada, California.

Q. And you are connected with Byron Jackson, are you not? A. Yes, sir.

Q. How long have you been connected with that company? A. About twelve years.

Q. In what capacity?

A. As manager of the patent and new development department.

Q. What has been your experience along those lines? A. With the Byron Jackson Company?

Q. Yes.

A. It is my duty to watch all of the patents that issue each week from the Patent Office, of which there are 700 to 1000 a week, and to interview inventors and promoters who think they have something which might be of interest to the Byron Jackson Company; to make an analysis of those patents which seem to be in our line of business, to determine whether the patent covers anything of material value, whether it might stand up in litigation, and to determine questions of validity and infringement, and then to go into the cost of manufacture of the product, and the question of whether they can be manufactured in our plant; to make a survey of the market, the probable price that can be obtained, and to determine, finally, whether or not a profit can be made on the item; and to determine whether it can be sold through our existing sales facilities or would require some extension of those facilities.

Q. Had you ever had any experience in patents and inventions before coming to Byron Jackson?

(Testimony of John Chesnut.)

A. Yes, sir.

Q. Where, and how much?

A. I was with the Standard Oil Company of California from 1920 to 1930, and during the first five years I was in the engineering department of the Standard Oil Company in San Francisco, that is, the general engineering department. The last five years I was assistant manager of their Patent Department.

Q. What university did you graduate from?

A. I didn't graduate. I attended the University of California for two years.

Q. You have heard the testimony in this case, have you not? A. Yes, sir.

Q. And you have heard described the different inven- [286] tions that Mr. Ballagh and Mr. Miller have claimed to have made? A. Yes, sir.

Q. As to how many of those claimed inventions are *their* competitive devices?

Mr. Bednar: May I ask a question on voir dire?

Mr. Lamont: Yes.

Q. By Mr. Bednar: In all this investigation, Mr. Chesnut, did you investigate anything other than field devices that you use in your own business?

A. Yes; I investigated the products made by any company with which we are affiliated or in which we have any financial interests. I have made it a practice to watch the rubber items that could be sold in the oil fields, because we have a substantial interest in the Patterson-Ballagh Corporation.

Q. Do you know anything about the amount of

(Testimony of John Chesnut.)

competition with respect to these items you are going to testify to? A. In a general way.

Mr. Lamont: Now, will you read my last question, Mr. Reporter?

(Question read.)

A. I believe all of them, except possibly one or two, in which there has been a very, very limited sale. I refer to the steel clad protector and the plastic sucker rod protector and tubing protector.

[287]

Q. Referring to the same inventions, are any of those claimed inventions of an extraordinary nature?

Mr. Bednar: Just a minute. May I have that question read?

(Question read by the reporter)

Mr. Bednar: I object to that as calling for a conclusion of the witness.

Mr. Lamont: My purpose in going into this is to show that they are simply, you might say, run of the mill inventions with respect to anything of this type of any similar company.

Mr. Bednar: I don't think it is important whether they are patentable.

Mr. Lamont: I am asking him about the inventions.

Mr. Bednar: That is very uncertain.

The Court: You are asking now whether they are extraordinary. I don't know about that.

Q. By Mr. Lamont: What is the nature of these inventions as a whole, we will say?

Mr. Bednar: I think that is generalizing. If

(Testimony of John Chesnut.)

you are going to talk about competing items, why not limit yourself to one item.

Mr. Lamont: I am talking about these inventions that are being claimed.

Mr. Bednar: I object to it as calling for a conclusion and opinion of this witness.

The Court: I don't know about that word "extraordinary." What might be extraordinary to one man wouldn't be to another.

Mr. Lamont: I rephrased my question.

The Court: I didn't hear that. What is it now?

Mr. Lamont: Please read the last question.

(Question read by the reporter.)

The Court: All right. You may answer.

A. As a preface to the answer to that question, I might say that in connection with my qualifications I failed to state that I am a registered patent attorney and that I am quite familiar with the values of patents as such. And, looking at these inventions from the standpoint of a patent which could be enforced to protect a valuable monopoly, and also looking at possible markets for the invention——

Mr. Bednar: I don't want to interrupt, but I don't think the man is qualified to testify.

The Court: I don't know. He was asked a question and he hasn't answered it. Read the question.

(Question read by the reporter.)

Mr. Bednar: I object to the question.

The Court: He may answer the question.

(Testimony of John Chesnut.)

A. I would say that they are well described by the term "run of the mill inventions." They relate to minor improvements, and probably useful improvements in inventions or in devices made by a specialty manufacturer, which includes rubber products in the oil industry, and in any [289] business we expect the manufacturer will improve his products from time to time and find other items which fit into his line, and I would say they are just average inventions, if they are inventions.

Q. By Mr. Lamont: Now referring to this invention of the lip protector, have you ever heard of a patent on that particular——

A. No, sir.

Q. Is it patentable?

A. Not in my opinion.

Mr. Bednar: Objected to as calling for a conclusion of the witness.

Mr. Lamont: He is an expert along that line. He is a registered patent attorney and experienced in that line.

The Court: In patent cases they can testify to anything, and this really is a patent case. This was patented?

Mr. Lamont: An application was filed. A patent was not issued.

The Court: That is right. He may answer.

A. In my opinion, it is not patentable at all, or, if any claim should be allowed by the Patent Office, it would be of a very limited nature. I base that

(Testimony of John Chesnut.)

opinion upon a study of prior patents, for instance, a patent to a man by the name of Berryman.

Q. By Mr. Lamont: Let me ask you whether this is [290] the Berryman patent that I now hand you. A. Yes, sir.

Q. Will you continue with your answer?

A. Berryman patent No. 1,913,018, issued June 6, 1933, shows a casing protector having a streamlined lip at either end. It differs from the Patterson-Ballagh protector mainly in that this is of the so called split protector type, instead of being a solid ring like the Patterson-Ballagh protector, but in so far as a lip protector is concerned, it is immaterial whether the protector is split or solid, and in my opinion the lip of the Berryman patent would be sufficient to prevent the issuance of another patent upon the Patterson-Ballagh protector based solely upon the streamlining of that lip and the elimination of eddy currents which might groove the pipe. The second advantage, or alleged advantage, of the Patterson-Ballagh lip protector is that it sticks to the pipe better, but in my opinion that is due solely to the length of the protector, and the Patterson-Ballagh lip protector is longer by the length of the lip, and therefore has just that much better grip on the pipe. That would also be true of this Berryman protector, and I don't see anything that you could base patentability on on the length of the lip. The third advantage, as to whether or not the lip prevents splitting of the protector, that, I think, is a question of degree,

(Testimony of John Chesnut.)

a question of the relative length of that lip. We have a [291] prior patent, I believe to a man named Bettis.

Mr. Lamont: Yes. Before we proceed with this patent, I desire to place this Berryman patent in evidence.

The Clerk: Plaintiff's Exhibit 21.

Q. By Mr. Lamont: Now I hand you another patent, and ask you whether that is the patent you referred to.

A. Yes, sir. This is Bettis patent No. 2,166,937, issued July 25, 1939. It shows a solid ring protector, in which there is what might be termed a lip 8 at each end of the protector, and in my opinion this lip 8 would serve the same purpose as the lip on the Patterson-Ballagh protector, to the extent that its length is equal to or approaches that of the Patterson-Ballagh protector. In my opinion, I don't believe patentability of the lip of the Patterson-Ballagh protector—I should say that I don't believe that the lip on the Patterson-Ballagh protector is patentable over the lip shown in this Bettis patent.

Q. There is one other patent?

A. There is one other patent which has a bearing on this question, and that is the patent to Smith, which shows a streamlined protector. It doesn't have a lip in the sense of having any abrupt change in the thickness of the protector, but it does show a protector which is generally streamlined from one

(Testimony of John Chesnut.)

end to the other, to reduce the eddy currents to a minimum.

Mr. Lamont: I will offer this Bettis patent in evidence. [292]

Q. By Mr. Lamont: I now show you another patent and ask you whether that is the Smith patent.

The Clerk: The Bettis patent will be Plaintiff's Exhibit 22.

A. Yes, sir. This is Smith patent No. 2,197,531, issued April 16, 1940, and shows a streamlined protector.

Mr. Lamont: I will offer this patent in evidence.

The Clerk: That will be Plaintiff's Exhibit 23.

Q. By Mr. Lamont: With regard to pipe wipers, what was the first patent in time having to do with pipe wipers? A. The Penfield patent.

Q. The Ballagh patent, apparently the application was filed after that time, was it?

A. Yes, sir.

Q. Now let me ask you this. Are the claims of the Ballagh patent broad or basic, in the sense that they would control or monopolize the market?

A. No, sir. They are limited to the specific construction used in the Patterson-Ballagh pipe wiper, and in my opinion would not be infringed, for example, by the Bettis or Penfield device.

Q. Will you state briefly your conclusions as to the sucker rod protector, the open hole protector, and the other items mentioned?

A. Taking the sucker rod protector and tubing protector together, since they are generally used

(Testimony of John Chesnut.)

under the same conditions, [293] I would say that the market for such devices is very limited, generally limited to wells of very great depth, as Mr. Ballagh pointed out, or to very crooked wells such as were drilled many years ago, but which we do not encounter today, or wells that are intentionally drilled at a slant, such as the tide lands they were drilling down at Huntington Beach, California, which are drilled at quite an angle to the vertical, and in those instances there might be occasion to use sucker rod protectors and tubing protectors, but in my opinion the total market as compared to protectors of all types is very small, and there have been many inventors who have worked in that field, and many patents have been taken out showing tubing and rod protectors composed of material other than rubber. There is, for example, the Conrader patent. Do you have the Conrader patent there? I would like to have it.

Q. Yes; I have that here.

A. This is Conrader patent No. 831,143, issued September 18, 1906. It shows a protector mounted upon a tubular sucker rod, and for the purpose of patentability I would say that that protector is the equivalent of either a rod protector or a tubing protector, and it is slideable up and down freely on the rod, as is the rod protector of the Patterson-Ballagh Corporation. This patent doesn't say what the material is that the sleeve is composed of. It could be metal or some other material. There are, however, [294] patents showing bakelite, wood,

(Testimony of John Chesnut.)

bronze, and other materials used for protectors of this general type. The interesting thing about this is that it shows a protector that has a wearing surface both inside and outside, and because of the existence of this Conrader patent I would say that no one today could get another patent on the general idea of such a protector. They might, of course, get a patent on some particular material which could be used, but the value of that patent would depend on how much superior that material would be over any other material suitable for that purpose.

Mr. Lamont: I offer that patent in evidence.

The Clerk: It will be Plaintiff's Exhibit 24.

Q. By Mr. Lamont: The next patent I show is the Ballagh patent, which is on the drill pipe wiper.

A. Yes, sir. Patent No. 2,272,395, issued February 10, 1942, filed May 29, 1939.

Mr. Lamont: I will offer this Ballagh patent in evidence.

The Witness: You referred to the Penfield patent, did you not?

The Clerk: That is already in.

Q. By Mr. Lamont: You referred to the Penfield patent? A. Yes, sir.

Q. Is that the patent you have in mind?

A. Yes; this is the patent, No. 2,215,377, issued September 17, 1940, and filed May 2, 1939, which is about [295] a month prior to the filing date of the Ballagh patent.

(Testimony of John Chesnut.)

Mr. Lamont: I will offer this patent in evidence. The Ballagh patent is apparently not in evidence.

The Clerk: The Penfield patent will be Plaintiff's Exhibit 25.

Mr. Lamont: I next offer the Ballagh patent as Plaintiff's Exhibit 26.

Q. By Mr. Lamont: I just have one more patent, the Woods patent. What bearing has that, if any, on those inventions?

A. Woods patent No. 1,764,769, issued June 17, 1930, shows a drill pipe protector which is, in its principal characteristics, similar to the open hole or steel clad protector on which Mr. Miller has filed a patent application. In the Woods patent there is a metal or steel sleeve surrounding a groove in the tool joint. That steel sleeve is rotatable upon the tool joint, and is held in place by means of a soft metal, in this case bronze, to keep the rotatable sleeve from falling off of the tool joint. In the Miller device, the open hole protector, rubber is used in place of the bronze of this patent, and there is a further difference that the Miller device is intended to be placed upon the drill pipe at some point other than the tool joint. I would say that the general idea of having a rotatable sleeve made of steel to withstand abrasion in an open hole and secured in place by some softer metal or material which will resist wear [296] better than steel, is shown by the Woods patent, and therefore any patent that may issue upon Mr. Miller's steel clad protector would have to be limited to the minor details

(Testimony of John Chesnut.)

of construction by which he is enabled to apply the protector to the drill pipe rather than to the tool joint. Whether or not the trade would prefer to have it in that position is an open question. Generally they want the protector to be at the tool joint, as close to it as you can get it. My main conclusion is that the Miller invention, if patentable, is only patentable to a very limited degree.

Mr. Lamont: I offer this patent in evidence.

The Clerk: Plaintiff's Exhibit 27.

Mr. Lamont: You can take the witness.

The Court: We will have our afternoon recess at this time.

(Short recess.)

Mr. Bednar: No cross examination.

Mr. Lamont: That is all. That is our case. Have you anything further?

Mr. Bednar: Nothing further.

Mr. Lamont: That is the story. I would like to ask now what the Court desires, whether it desires oral argument or briefs, or what.

The Court: Whichever you gentlemen choose.

Mr. Bednar: I prefer just oral argument.

Mr. Lamont: I prefer that, if it can come up at some [297] other time, so that I will have a chance to check up my notes and all that.

The Court: We can probably arrange a day. There isn't anything set tomorrow, is there, Mr. Cross?

Mr. Lamont: Tomorrow would be more than sat-

isfactory to me, because then I wouldn't have to make another trip down here.

The Clerk: Just the sentence, your Honor, in the Jones case, which was heard before you.

The Court: Come in at 10:00 o'clock, then.

Mr. Lamont: May I ask, are we going to have a limited time? In arranging an argument, I like to know how much time the Court expects us to consume.

The Court: How much time do you desire?

Mr. Lamont: I think I can get through in half an hour.

Mr. Bednar: Half an hour is all I want.

Mr. Lamont: We can have a tentative understanding that it will be about a half hour on a side.

The Court: I will leave it up to you gentlemen. Talk as long as you have anything to say.

Mr. Lamont: And don't talk any longer?

The Court: And don't talk any longer.

The Clerk: May the record show that Plaintiff's Exhibits 3 and 18, heretofore missing, have been replaced by duplicate exhibits, with the same numbers?

The Court: Yes. Is that all? [298]

The Clerk: Yes, your Honor.

[Endorsed]: Filed November 16, 1942. [299]

[Endorsed]: No. 10473. United States Circuit Court of Appeals for the Ninth Circuit. Byron Jackson Co., a corporation, Appellant, vs. Patterson-Ballagh Corporation, a corporation, J. C. Ballagh and D. G. Miller, Appellees. Transcript of Record. Upon Appeal from the District Court of the United States for the Southern District of California, Central Division.

Filed June 21, 1943.

PAUL P. O'BRIEN,
Clerk of the United States Circuit Court of Appeals for the Ninth Circuit.

In the United States Circuit Court of Appeals
for the Ninth Circuit

No. 10473

BYRON JACKSON CO., a corporation,
Plaintiff and Appellant,

vs.

PATTERSON-BALLAGH CORPORATION, a corporation, J. C. BALLAGH and D. G. MILLER,
Defendants and Appellees.

CONCISE STATEMENT OF POINTS UPON WHICH APPELLANT INTENDS TO RELY ON APPEAL

Pursuant to the provisions of Rule 19(6) of the Circuit Court of Appeals for the Ninth Circuit,

Byron Jackson Co., a corporation, appellant, hereby files a concise statement of the points upon which it intends to rely on appeal, as follows:

1. The District Court erred in not finding that the persons who were and had been directors of defendant Patterson-Ballagh Corporation since February 15, 1939, (other than the defendant Ballagh, the defendant Miller, and E. S. Dulin) in fact were selected by and were in fact representatives of the said Ballagh and the said Miller upon the said Board.

2. The District Court erred in not finding that the said Ballagh and the said Miller ever since February 15, 1939, dominated, controlled, and directed each and every of the acts and doings of said Patterson-Ballagh Corporation.

3. The District Court erred in finding that since February 15, 1939, the said Ballagh and the said Miller, pursuant to or subject to the instructions, advice, supervision or direction of the Board of Directors of said Patterson-Ballagh Corporation, directed the affairs of said Patterson-Ballagh Corporation or carried on its business.

4. The District Court erred in finding that said Ballagh and said Miller, or either thereof, have discharged their duties as such officers faithfully, efficiently, or conscientiously or loyally or meritoriously as to the payment of salaries and/or remuneration to themselves.

5. The District Court erred in not finding that the said Ballagh and the said Miller at all times since February 15, 1939, fraudulently and unlaw-

fully connived, cooperated, schemed, and conspired in directing the affairs of said Patterson-Ballagh Corporation for their own ends (as distinguished from the well-being of said corporation and the interests of plaintiff as a minority stockholder), and for their own profit.

6. The District Court erred in not finding that the said Ballagh and the said Miller declared and paid to the said Ballagh grossly excessive salaries and compensation for services rendered by the said Ballagh to said Patterson-Ballagh Corporation.

7. The District Court erred in not finding that the salary and compensation paid to the said Ballagh for the calendar year 1939 was grossly excessive in at least the amount of $3,000.

8. The District Court erred in not finding that the salary and compensation paid to the said Ballagh for the calendar year 1940 was grossly excessive in at least the amount of $18,166.66.

9. The District Court erred in not finding that the salary and compensation paid to the said Ballagh for that part of the calendar year 1941 up to the time of the commencement of this action was grossly excessive in at least the amount of $9,000.

10. The District Court erred in not finding that the payment of the salaries to the said Ballagh and for the calendar years 1939, 1940, and 1941 was made as a part of a scheme and conspiracy to defraud, entered into by the said Ballagh and the said Miller.

11. The District Court erred in finding that the services rendered by the said Ballagh to Patterson-Ballagh Corporation from January 1, 1939 to the

time of filing suit on September 10, 1941, were and/or are now and/or will continue to be of very great value to Patterson-Ballagh Corporation.

12. The District Court erred in finding that the services of the said Ballagh were performed loyally, efficiently, carefully or effectively, as to the payment of salaries and/or remuneration to the said Ballagh and/or the said Miller.

13. The District Court erred in finding that the compensation paid to the said Ballagh for the periods set forth in paragraphs 7, 8, and 9 hereof was fair, just, or reasonable at the various times it was authorized or approved or paid.

14. The District Court erred in not finding that, by prior arrangement between the said Ballagh and the said Miller, the said Miller voted in favor of the said Ballagh upon all resolutions concerning the compensation of the said Ballagh.

15. The District Court erred in finding that any resolution concerning the compensation of the said Ballagh was approved in good faith and/or by an independent and/or disinterested majority of the directors present at such meeting.

16. The District Court erred in not finding that the compensation paid to the said Ballagh during the calendar year 1939 was approved and ratified at the annual meeting of the shareholders on January 16, 1940 only over and against the protest and objection of the plaintiff herein.

17. The District Court erred in not finding that the compensation paid to the said Ballagh during the calendar year 1940 was approved and ratified at

the annual meeting of the shareholders on January 21, 1941 only over and against the objection and protest of the plaintiff herein.

18. The District Court erred in not finding that the compensation paid to the said Ballagh from January 1, 1941 to September 10, 1941 was approved and ratified at the annual meeting of the shareholders on January 20, 1942 only over and against the objection and protest of the plaintiff herein.

19. The District Court erred in finding that the resolutions of stockholders, or any thereof, mentioned in paragraphs 16, 17, and 18 hereof, were regularly and/or legally adopted or adopted in good faith and/or without fraud by each and all, or any, of the stockholders voting for the same.

20. The District Court erred in not finding that the payment of the salaries to the said Miller and for the calendar year 1940 and for the calendar year 1941 prior to the time of the commencement of this suit was made as a part of a scheme and conspiracy to defraud, entered into by the said Ballagh and the said Miller.

21. The District Court erred in not finding that the sum of $19,750 paid to the said Miller for the calendar year 1940 was grossly excessive in at least the sum of $7750.

22. The District Court erred in not finding that the sum of $12,000 paid to the said Miller for that part of the calendar year of 1941 prior to the time of the commencement of this action was grossly excessive in at least the sum of $5,000.

23. The District Court erred in finding that the resolutions adopted by the Board of Directors of Patterson-Ballagh Corporation fixing compensation of the said Miller for services rendered by him to Patterson-Ballagh Corporation were duly, regularly and/or legally adopted by the Board of Directors of said corporation.

24. The District Court erred in finding that the services rendered by the said Miller to the Patterson-Ballagh Corporation from January 1, 1940 to the time of filing this action were and/or now are and/or will continue to be of substantial value to Patterson-Ballagh Corporation.

25. The District Court erred in finding that such services referred to in paragraph 24 hereof were performed loyally, efficiently, carefully, or effectively.

26. The District Court erred in finding that the compensation paid to the said Miller during the periods mentioned in paragraphs 21 and 22 hereof was fair, just, or reasonable as to Patterson-Ballagh Corporation at the various times it was authorized or approved or paid.

27. The District Court erred in not finding that, by prior arrangement between the said Ballagh and the said Miller, the said Ballagh voted in favor of the said Miller upon all resolutions concerning the compensation of the said Miller.

28. The District Court erred in finding that the resolutions, or any thereof, fixing the compensation of the said Miller were approved in good faith or

by an independent or disinterested majority of the directors present at such meetings.

29. The District Court erred in not finding that the compensation paid to the said Miller during the calendar year 1940 was approved and ratified at the annual meeting of the shareholders on January 21, 1941, only over and against the objection and protest of the plaintiff herein.

30. The District Court erred in not finding that the compensation paid to the said Miller from January 1, 1941 to September 10, 1941, was approved and ratified at the annual meeting of the shareholders on January 20, 1942, only over and against the objection and protest of the plaintiff herein.

31. The District Court erred in finding that the resolutions of stockholders or any part thereof mentioned in paragraph 29 and 30 hereof were regularly and/or legally adopted or adopted in good faith and/or without fraud by each and all or any of the stockholders voting for the same.

32. The District Court erred in not finding that the amount of the salaries and compensation of the said Ballagh and the said Miller were fixed with the purpose and intent of depriving the plaintiff of dividends accruing or to accrue to plaintiff from the said Patterson-Ballagh Corporation.

33. The District Court erred in not finding that, if said excessive salaries and compensation had not been paid to the said Ballagh and the said Miller, such excess would have been available for the payment of dividends to the stockholders of Patterson-Ballagh Corporation, including the plaintiff.

34. The District Court erred in not finding that the amount of the salaries and compensation to the said Ballagh and the said Miller were neither fairly nor honestly determined by the said Ballagh and the said Miller.

35. The District Court ererd in not finding that for and on acount of the payment of excessive salaries and compensation the defendants Ballagh and Miller are indebted to said Patterson-Ballagh Corporation in at least the sum of $41,416.66, no part of which has been repaid by the said Ballagh and the said Miller, or either thereof, to the said corporation.

36. The District Court erred in not finding that plaintiff failed to obtain any action by the directors or the stockholders of Patterson-Ballagh Corporation due to the domination, control, and direction of said corporation by the said Ballagh and the said Miller, and due to a scheme and conspiracy to defraud, entered into by the said Ballagh and the said Miller.

37. The District Court erred in finding that, prior to the participation in and approving of the election of H. C. Armisted, Howard Burrell, J. C. Ballagh and D. G. Miller as directors and officers on June 21, 1941, the said Dulin knew the attitude of said persons concerning the compensation that said persons considered should properly be paid to the said Ballagh and the said Miller during 1941.

38. The District Court erred in finding that plaintiff has waived any right it might have to complain of the compensation paid to the said Bal-

lagh and/or the said Miller by Patterson-Ballagh Corporation from January 1, 1941, to the time of filing suit herein on September 10, 1941.

39. The District Court erred in concluding, as a conclusion of law, that the compensation paid by Patterson-Ballagh Corporation to the said Ballagh from January 1, 1939 to the time of filing suit herein has been fair, just, or reasonable as to said corporation at the various times it was authorized, approved, or paid.

40. The District Court erred in concluding, as a conclusion of law, that the compensation paid by Patterson-Ballagh Corporation to the said Miller from January 1, 1940 to the time of filing suit herein was fair, just, or reasonable as to said corporation at the various times it was authorized, approved, or paid.

41. The District Court erred in concluding, as a conclusion of law, that plaintiff has waived any right to complain of the compensation paid by Patterson-Ballagh Corporation to the said Ballagh and/or the said Miller from January 1, 1940 to the time of filing suit herein.

42. The District Court erred in concluding, as a conclusion of law, that plaintiff has waived any right to complain of the compensation paid by Patterson-Ballagh Corporation to the said Ballagh and the said Miller from January 1, 1941 to the time of filing said suit herein on September 10, 1941.

43. The District Court erred in finding that plaintiff is not entitled either on its own behalf or

on behalf of Patterson-Ballagh Corporation to any relief or recovery whatsoever against any of said defendants.

44. The District Court erred in finding that the defendants herein, or any of said defendants, are entitled to recovery of or from plaintiff their, his, or its respective costs of suit herein incurred.

45. The District Court erred in ordering that judgment be entered in favor of the defendants.

46. If the District Court, in determining the value of the services of the said Ballagh to Patterson-Ballagh Corporation, or in determining that the salary and/or compensation of the said Ballagh for services to Patterson-Ballagh Corporation was not excessive, took into consideration the value of any claimed services rendered by him as an inventor or as the patentee of any inventions or as the applicant for any patent or the value of any inventions or of any patents or of any applications for patents of the said Ballagh, whether or not assigned to Patterson-Ballagh Corporation, the said District Court erred in so doing.

47. If the District Court, in determining the value of the services of the said Miller to Patterson-Ballagh Corporation, or in determining that the salary and/or compensation of the said Miller for services to Patterson-Ballagh Corporation was not excessive, took into consideration the value of any claimed services rendered by him as an inventor or as the patentee of any inventions or as the applicant for any patent or the value of any inventions or of any patents or of any applications for patents

of the said Miller, whether or not assigned to Patterson-Ballagh Corporation, the said District Court erred in so doing.

For each and all of the above reasons the District Court erred in finding and determining that appellees were entitled to judgment as rendered.

Dated, June 21, 1943.

CHICKERING & GREGORY,
DONALD Y. LAMONT,
FREDERICK M. FISK,
111 Sutter Street,
San Francisco, California.
LYON & LYON,
LEONARD S. LYON,
IRWIN L. FULLER,
811 West Seventh Street,
Los Angeles, California.
Attorneys for Plaintiff and Appellant.

Service of a copy of the within points to be relied upon is hereby acknowledged this 21st day of June, 1943.

MUSICK, BURRELL & PINNEY,
By A. B. JACKSON,
Attorneys for Defendants and Appellees.

[Endorsed]: Filed June 23, 1943; Paul P. O'Brien, Clerk.

[Title of Circuit Court of Appeals and Cause]

DESIGNATION BY APPELLANT, BYRON JACKSON CO., A CORPORATION, OF THE PARTS OF THE RECORD SAID APPELLANT THINKS NECESSARY FOR THE CONSIDERATION OF THE POINTS ON WHICH IT INTENDS TO RELY ON APPEAL.

Pursuant to Rule 19 (6) of the Circuit Court of Appeals for the Ninth Circuit, Byron Jackson Co., a corporation, the appellant above named, hereby designates the following parts of the record which it thinks necessary for the consideration of the points upon which it intends to rely on the appeal, to-wit: the entire record.

The appellant requests that the entire record be printed except such parts as the printing thereof may hereafter be dispensed with by stipulation and appropriate order, or by appropriate order, and appellant furthermore requests that such parts of said

record, the printing of which may hereafter be dispensed, be not printed.

Dated, June 21, 1943.

CHICKERING & GREGORY,
DONALD Y. LAMONT,
FREDERICK M. FISK,
111 Sutter Street,
San Francisco, California.
LYON & LYON,
LEONARD S. LYON,
IRWIN L. FULLER,
811 West Seventh Street,
Los Angeles, California.
Attorneys for Appellant.

Service of a copy of the within Designation is hereby acknowledged this 21st day of June, 1943.

MUSICK, BURRELL & PINNEY,
By A. B. JACKSON,
Attorneys for Defendants-Appellees.

[Endorsed]: Filed June 23, 1943; Paul P. O'Brien, Clerk.

[Title of Circuit Court of Appeals and Cause.]

STIPULATION

It Is Hereby Stipulated and Agreed by and between plaintiff-appellant and defendants-appellees, this Honorable Court approving and consenting thereto, that in printing the record in the above entitled cause the Clerk shall omit therefrom the following documents and exhibits:

> The defendant company's financial statements, Exhibits 6a, 6b and 6c, respectively, offered and received in evidence upon the trial of said cause, because of the difficulty and expense in printing the same and the further fact that the court will not be required to make a minute study of the same;

It Is Further Stipulated that the documents and exhibits above mentioned to be ommitted from the printed record shall nevertheless still constitute a part of the record to be considered by the court and shall be preserved by the court and may be referred to by counsel or the court, if deemed necessary, during the course of the argument or otherwise during the disposition of the cause as fully and to the same extent and with the same force and effect as if said documents and exhibits were printed in full in the printed record herein;

It Is Further Stipulated that in the event counsel for defendants-appellees, in the preparation of their brief, shall deem it necessary to inspect or

examine any of the aforesaid Exhibits, counsel for plaintiff-appellant, upon request by counsel for defendants-appellees will endeavor to obtain an order from this court to withdraw said Exhibits for such purpose.

Dated this 2nd day of July, 1943.

DONALD Y. LAMONT,
LEONARD S. LYON,
IRWIN L. FULLER,
Attorneys for Plaintiff-Appellant.
MUSICK, BURRELL & PINNEY,
By A. B. JACKSON,
Attorneys for Defendants-Appellees.

The Foregoing Stipulation Is Hereby Approved and It Is So Ordered this 7th day of July, 1943.

FRANCIS A. GARRECHT,
U. S. Circuit Judge.

[Endorsed]: Filed July 7, 1943. Paul P. O'Brien, Clerk.

[Title of Circuit Court of Appeals and Cause.]

STIPULATION

It Is Hereby Stipulated and Agreed by and between plaintiff-appellant and defendants-appellees, this Honorable Court approving and consenting thereto, that in printing the record in the above entitled cause the Clerk shall omit therefrom the following documents and exhibits:

(1) The depositions of J. C. Ballagh, D. G. Miller and E. S. Dulin, including all exhibits thereto save and except such exhibits as were offered and received in evidence upon the trial of said cause. These depositions were not offered or received in evidence and therefore are not a part of the record;

(2) Plaintiff's Exhibits 5a, 5b and 5c (the Pennington-Swanson audits) because of the difficulty and expense in printing the same;

(3) All letters patent, being plaintiff-appellant's Exhibits 17a, 17b, 20, 21, 22, 23, 24, 25, 26 and 27, and defendants-appellees' Exhibit H, because of the expense of printing and the further fact that the court will not be required to make a minute study of the same;

(4) All catalogues and parts thereof, being defendants-appellees' Exhibits E and O, because of the expense of printing and also upon the further fact that they will be of more aid to the court in their original form;

(5) All photographs, being defendants-appellees'

Exhibits J, K and M, because of the expense of reproduction thereof;

(6) All charts, being plaintiff-appellant's Exhibits 18a, 18b, 18c and 18d, and defendants-appellees' Exhibits A, B, F and G, because of the expense and the fact that the charts will be very difficult to reproduce due to the use of colors and due to the size thereof, and also to the fact that the court can obtain a much better understanding by an examination of the originals.

It Is Further Stipulated that the documents and exhibits above mentioned to be omitted from the printed record shall, (except as to the depositions referred in Item (1) above and which are not a part of the record, not having been offered in evidence) nevertheless still constitute a part of the record to be considered by the court and shall be preserved by the Court and may be referred to by counsel or the Court, if deemed necessary, during the course of the argument or otherwise during the disposition of the cause as fully and to the same extent and with the same force and effect as if said documents and exhibits were printed in full in the printed record herein;

It Is Further Stipulated that in the event counsel for defendants-appellees, in the preparation of their brief, shall deem it necessary to inspect or examine any of the aforesaid Exhibits, counsel for plaintiff-appellant, upon request by counsel for defendants-

appellees will endeavor to obtain an order from this Court to withdraw said Exhibits for such purpose.

Dated this 29th day of June, 1943.

DONALD Y. LAMONT,
LEONARD S. LYON,
IRWIN L. FULLER,
Attorneys for Plaintiff-Appellant.
MUSICK, BURRELL & PINNEY,
HOWARD BURRELL, ANSON B. JACKSON, Jr.,
H. W. MATTINGLY,
Attorneys for Defendants-Appellees.

The Foregoing Stipulation Is Hereby Approved and It Is So Ordered this 30th day of June, 1943.

FRANCIS A. GARRECHT,
U. S. Circuit Judge.

[Endorsed]: Filed Jul 1, 1943. Paul P. O'Brien, Clerk.

No. 10,473

IN THE

United States Circuit Court of Appeals

For the Ninth Circuit

BYRON JACKSON CO., a corporation,
Appellant,

vs.

PATTERSON-BALLAGH CORPORATION, a corporation, J. C. BALLAGH and D. G. MILLER,
Appellees.

BRIEF FOR APPELLANT.

CHICKERING & GREGORY,
DONALD Y. LAMONT,
FREDERICK M. FISK,
STEPHEN R. DUHRING,
111 Sutter Street, San Francisco, California,
LYON & LYON,
LEONARD S. LYON,
IRWIN L. FULLER,
810 West Seventh Street, Los Angeles, California,
Attorneys for Appellant.

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Texts

No. 10,473

IN THE

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BYRON JACKSON CO., a corporation,
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vs.

PATTERSON-BALLAGH CORPORATION, a corporation, J. C. BALLAGH and D. G. MILLER,
Appellees.

BRIEF FOR APPELLANT.

STATEMENT OF THE PLEADINGS AND FACTS DISCLOSING THE BASIS FOR JURISDICTION.

The pleadings involved in the case at bar consist of plaintiff's complaint (R., 2), defendants' motion to dismiss the complaint (R., 15) defendants' answer (R., 17) and defendants' amendment to the answer (R., 29).

The action was brought by plaintiff in the United States District Court for the Southern District of California, Central Division. The plaintiff was a corporation of the State of Delaware and a citizen and resident of that state. The defendants were all citizens and residents of the Central Division of the Southern District of California, the defendant Patterson-

Ballagh Corporation being a corporation organized and existing under the laws of the State of California. The action involved a sum or value in excess of Three Thousand Dollars ($3,000) exclusive of interest and costs (R., 9; 60). Jurisdiction of such action was vested in the United States District Court by Section 24(1) of the Judicial Code (U.S.C.A., Title 28, Sec. 41(1)).

This proceeding being an appeal from the final decision of the United States District Court in said matter (R., 84), jurisdiction is vested in this honorable United States Circuit Court of Appeals for the Ninth Circuit by Section 128(a) of the Judicial Code (U.S.C.A., Title 28, Sec. 225, Subd. (a)).

CONCISE STATEMENT OF THE CASE.

This case was tried before Mr. Judge Dave W. Ling without a jury. He decided in favor of the defendants. No opinion was written.

The action was commenced to enforce secondary rights on the part of the plaintiff as a minority stockholder in Patterson-Ballagh Corporation (hereinafter sometimes called the "Corporation"), because the Corporation refused to enforce such rights against Ballagh and Miller who were the majority stockholders and to whom plaintiff claimed the Corporation had been paying (during the years 1939, 1940 and 1941) excessive salaries (R. 2). Although the Corporation is named as a defendant, the action is one

for and on behalf of the Corporation and, therefore, the term "defendants" as hereinafter used is intended only to include the defendants Ballagh and Miller.

The Corporation was organized in September of 1928 to take over the business of a theretofore existing partnership in which the defendant Ballagh and one C. L. Patterson were the sole partners (R., 61; 476; 477). That partnership had been engaged in the manufacture and sale of so-called "casing protectors" which were claimed to be patented and which were used in the drilling of oil wells.[1] The Corporation, after its formation, engaged in the manufacture and sale of products for use in the drilling of oil wells and very largely in the manufacture and sale of casing protectors as theretofore manufactured by the partnership or as slightly modified.

At the time of the formation of the Corporation there were issued 1,000 shares of its capital stock, which have ever since remained outstanding. No additional shares have ever been issued. Ballagh became the owner of 500 of said shares and Patterson became the owner of the remaining 500 thereof (R., 61).

Shortly after the formation of the Corporation and on or about September 20, 1928, the plaintiff, the Cor-

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[1]A casing protector was a simple device and was defined by Ballagh as follows: "A casing protector is a continuous ring of rubber which has an inside diameter smaller than the inside diameter of the drill pipe on which it is to operate. It is forced over the drill pipe and fuses itself upon the drill pipe by the resilience of the rubber, and in that position has a diameter that is larger than that of the tool joint, and acts as a bearing medium to prevent the wearing or whipping of the tool joint against the casing." (R., 343.)

poration, Ballagh and Patterson entered into certain agreements which were introduced in evidence as Exhibits 15a, 15b, 15c, and 15d (R., 307-330). Under these agreements the Corporation was to pay to plaintiff certain royalties on casing protectors. Furthermore, under these agreements plaintiff was to purchase from Ballagh 125 shares of the stock of the Corporation and also from Patterson 125 shares of the stock of the Corporation. These purchases were made and, since September 20, 1928, the plaintiff has been the owner of 250 shares (R., 331-332; 340; 410). Ballagh continued to be the owner of 375 shares, except that in August of 1931 he conveyed 250 of his shares to a company in which he and his wife were the sole stockholders and which company thereafter continued to be the holder of said shares. Patterson continued to be the owner of 375 shares until February of 1939, at which time the defendant Miller became the beneficial owner of all of the Patterson stock (R., 61; 331-332; 340). Thus, during the period material to the present suit Ballagh was the beneficial owner of 375 shares, Miller the beneficial owner of 375 shares, and the plaintiff the owner of 250 shares.

At the time that Miller acquired the Patterson shares, or shortly thereafter, the Board of Directors of the Corporation was revamped, in a manner dictated by Ballagh and Miller, and thereafter consisted of Ballagh, Miller, one Howard Burrell (who about that time and by the selection of the defendants became the attorney for the Corporation (R., 429-430)), one H. C. Armington (an employee of the Corpora-

tion), and E. S. Dulin, plaintiff's president[2] (R., 352-354). Miller, in place of Patterson, became the President and General Manager (R., 62; 373) and Ballagh continued as Secretary and Treasurer and Sales Manager (R., 62; 483). According to the minutes which appear in evidence as Exhibit 1 (R., 206-267), the defendants were employed only in the capacities above stated. They were not employed as research men or inventors.

The new Board was dominated by Ballagh and Miller. These gentlemen dictated the policies of the Corporation (R., 354; 381; 399).

The new Board, over the objection of plaintiff as represented by Dulin, and almost immediately after its formation, did three things of importance: (1) it repudiated all obligation to pay plaintiff royalties under Exhibits 15a, 15b, 15c, and 15d (R., 222; 229; 336; 359; 382); (2) although dividends had theretofore been paid, and often in large amounts, it refused to pay any further dividends (R., 68; 245; 255; 284; 382); and (3) it made marked increases in the salaries of Ballagh and Miller, on account of which salaries the present action is being maintained.

For the calendar year 1939 Ballagh received as salary $15,000; for the calendar year 1940, $30,166.66; and for the part of the calendar year 1941 prior to the commencement of the present suit, which was September 10, 1941, $19,000 (R., 64). For the calendar year 1940 Miller received $19,750, and for such part of the

[2]Dulin could not be dislodged; there was cumulative voting.

calendar year 1941 prior to the commencement of this suit $12,000 (R., 66).[3]

Plaintiff claimed and does now claim that $12,000 per annum to each of the defendants was the outside, and the extreme outside, limit that the defendants by any stretch of the imagination could have justified as salaries. Plaintiff claimed and now claims that the defendants should reimburse the Corporation on account of excessive salaries paid prior to the commencement of the above entitled action in at least the sum of $41,416.66, together with interest.

Although the defendants in the trial court did not expressly concede that they were forced to resort to their claimed services as inventors in order to justify the amounts of their salaries, they did in several ways impliedly make such a concession.

The plaintiff in its complaint charged that defendants' salaries were excessive and that the Corporation was entitled to recover $41,416.66. The allegations that defendants' salaries were excessive were denied by the defendants in their answer. Thus the excessiveness of the salaries was put in issue.

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[3]The above salary figures were taken from the findings of the Court. These figures are for 1941 higher than the figures set forth in the complaint. They also vary from the figures for the Corporation's fiscal years which ended upon November 30. According to the Corporation's statements (Ex. 6) the following salaries were paid: For the fiscal year ending November 30, 1939, Ballagh received $15,500; for the fiscal year 1940—$29,166.66, and for the fiscal year 1941, up to September 10 of that year, $21,000. For the fiscal year 1940 Miller received $19,252, and for the fiscal year 1941, up to September 10, $13,500. For the entire fiscal year 1941 Ballagh and Miller together received $53,667 (R., 277-283) (Ex. 18D).

In their amendment to their answer, defendants set forth as an affirmative defense that plaintiff by its actions at stockholders' and directors' meetings had waived any claim as to the excessiveness of the salaries. Thus the question of waiver was put in issue.

The questions involved in this appeal are, therefore,

(a) Were the salaries of Ballagh and Miller excessive?

and

(b) Did the plaintiff waive its right to so claim?

SPECIFICATIONS OF ERROR RELIED UPON BY APPELLANT, AND THE REASONS WHY THE FINDINGS OF FACT AND CONCLUSIONS OF LAW ARE ALLEGED TO BE ERRONEOUS.

1. The District Court erred in not finding that the persons who were and had been directors of defendant Patterson-Ballagh Corporation since February 15, 1939, (other than the defendant Ballagh, the defendant Miller, and E. S. Dulin) in fact were selected by and were in fact representatives of the said Ballagh and the said Miller upon the said Board. There was substantial and ample evidence to support such a finding and there was no evidence to the contrary.

2. The District Court erred in not finding that the said Ballagh and the said Miller ever since February 15, 1939, dominated, controlled, and directed each and every of the acts and doings of said Patterson-Ballagh Corporation. There was substantial and ample evi-

dence to support such a finding and there was no evidence to the contrary.

3. The District Court erred in finding that since February 15, 1939, the said Ballagh and the said Miller, pursuant to or subject to the instructions, advice, supervision or direction of the Board of Directors of said Patterson-Ballagh Corporation, directed the affairs of said Patterson-Ballagh Corporation or carried on its business. There was no evidence to support this finding. The evidence was to the contrary.

4. The District Court erred in finding that said Ballagh and said Miller, or either thereof, have discharged their duties as such officers faithfully, efficiently, or conscientiously or loyally or meritoriously as to the payment of salaries and/or remuneration to themselves. There was no evidence to support this finding. The evidence was to the contrary.

5. The District Court erred in not finding that the said Ballagh and the said Miller at all times since February 15, 1939, fraudulently and unlawfully connived, cooperated, schemed, and conspired in directing the affairs of said Patterson-Ballagh Corporation for their own ends (as distinguished from the well-being of said corporation and the interests of plaintiff as a minority stockholder), and for their own profit. There was substantial and ample evidence to support such a finding and there was no evidence to the contrary.

6. The District Court erred in not finding that the said Ballagh and the said Miller declared and paid to the said Ballagh grossly excessive salaries and com-

pensation for services rendered by the said Ballagh to said Patterson-Ballagh Corporation. There was substantial and ample evidence to support such a finding and there was no evidence to the contrary.

7. The District Court erred in not finding that the salary and compensation paid to the said Ballagh for the calendar year 1939 was grossly excessive in at least the amount of $3,000. There was substantial and ample evidence to support such a finding and there was no evidence to the contrary.

8. The District Court erred in not findilng that the salary and compensation paid to the said Ballagh for the calendar year 1940 was grossly excessive in at least the amount of $18,166.66. There was substantial and ample evidence to support such a finding and there was no evidence to the contrary.

9. The District Court erred in not finding that the salary and compensation paid to the said Ballagh for that part of the calendar year 1941 up to the time of the commencement of this action was grossly excessive in at least the amount of $9,000. There was substantial and ample evidence to support such a finding and there was no evidence to the contrary.

10. The District Court erred in not finding that the payment of the salaries to the said Ballagh and for the calendar years 1939, 1940, and 1941 was made as a part of a scheme and conspiracy to defraud, entered into by the said Ballagh and the said Miller. There was substantial and ample evidence to support such a finding and there was no evidence to the contrary.

11. The District Court erred in finding that the services rendered by the said Ballagh to Patterson-Ballagh Corporation from January 1, 1939 to the time of filing suit on September 10, 1941, were and/or are now and/or will continue to be of very great value to Patterson-Ballagh Corporation. There was no evidence to support this finding. The evidence was to the contrary.

12. The District Court erred in finding that the services of the said Ballagh were performed loyally, efficiently, carefully or effectively, as to the payment of salaries and/or remuneration to the said Ballagh and/or the said Miller. There was no evidence to support this finding. The evidence was to the contrary.

13. The District Court erred in finding that the compensation paid to the said Ballagh for the periods set forth in paragraphs 7, 8, and 9 hereof was fair, just, or reasonable at the various times it was authorized or approved or paid. There was no evidence to support this finding. The evidence was to the contrary.

14. The District Court erred in not finding that, by prior arrangement between the said Ballagh and the said Miller, the said Miller voted in favor of the said Ballagh upon all resolutions concerning the compensation of the said Ballagh. There was substantial and ample evidence to support such a finding and there was no evidence to the contrary.

15. The District Court erred in finding that any resolution concerning the compensation of the said Ballagh was approved in good faith and/or by an independent and/or disinterested majority of the directors present at such meeting. There was no evidence to support this finding. The evidence was to the contrary.

16. The District Court erred in not finding that the compensation paid to the said Ballagh during the calendar year 1939 was approved and ratified at the annual meeting of the shareholders on January 16, 1940 only over and against the protest and objection of the plaintiff herein. There was substantial and ample evidence to support such a finding and there was no evidence to the contrary.

17. The District Court erred in not finding that the compensation paid to the said Ballagh during the calendar year 1940 was approved and ratified at the annual meeting of the shareholders on January 21, 1941 only over and against the objection and protest of the plaintiff herein. There was substantial and ample evidence to support such a finding and there was no evidence to the contrary.

18. The District Court erred in not finding that the compensation paid to the said Ballagh from January 1, 1941 to September 10, 1941 was approved and ratified at the annual meeting of the shareholders on January 20, 1942 only over and against the objection and protest of the plaintiff herein. There was substantial and ample evidence to support such a finding and there was no evidence to the contrary.

19. The District Court erred in finding that the resolutions of stockholders, or any thereof, mentioned in paragraphs 16, 17, and 18 hereof, were regularly and/or legally adopted or adopted in good faith and/or without fraud by each and all, or any, of the stockholders voting for the same. There was no evidence to support this finding. The evidence was to the contrary.

20. The District Court erred in not finding that the payment of the salaries to the said Miller and for the calendar year 1940 and for the calendar year 1941 prior to the time of the commencement of this suit was made as a part of a scheme and conspiracy to defraud, entered into by the said Ballagh and the said Miller. There was substantial and ample evidence to support such a finding and there was no evidence to the contrary.

21. The District Court erred in not finding that the sum of $19,750 paid to the said Miller for the calendar year 1940 was grossly excessive in at least the sum of $7750. There was substantial and ample evidence to support such a finding and there was no evidence to the contrary.

22. The District Court erred in not finding that the sum of $12,000 paid to the said Miller for that part of the calendar year of 1941 prior to the time of the commencement of this action was grossly excessive in at least the sum of $5000. There was substantial and ample evidence to support such a finding and there was no evidence to the contrary.

23. The District Court erred in finding that the resolutions adopted by the Board of Directors of Patterson-Ballagh Corporation fixing compensation of the said Miller for services rendered by him to Patterson-Ballagh Corporation were duly, regularly and/or legally adopted by the Board of Directors of said corporation. There was no evidence to support this finding. The evidence was to the contrary.

24. The District Court erred in finding that the services rendered by the said Miller to the Patterson-Ballagh Corporation from January 1, 1940 to the time of filing this action were and/or now are and/or will continue to be of substantial value to Patterson-Ballagh Corporation. There was no evidence to support this finding. The evidence was to the contrary.

25. The District Court erred in finding that such services referred to in paragraph 24 hereof were performed loyally, efficiently, carefully, or effectively. There was no evidence to support this finding. The evidence was to the contrary.

26. The District Court erred in finding that the compensation paid to the said Miller during the periods mentioned in paragraphs 21 and 22 hereof was fair, just, or reasonable as to Patterson-Ballagh Corporation at the various times it was authorized or approved or paid. There was no evidence to support this finding. The evidence was to the contrary.

27. The District Court erred in not finding that, by prior arrangement between the said Ballagh and the said Miller, the said Ballagh voted in favor of the said Miller upon all resolutions concerning the com-

pensation of the said Miller. There was substantial and ample evidence to support such a findilng and there was no evidence to the contrary.

28. The District Court erred in finding that the resolutions, or any thereof, fixing the compensation of the said Miller were approved in good faith or by an independent or disinterested majority of the directors present at such meetings. There was no evidence to support this finding. The evidence was to the contrary.

29. The District Court erred in not finding that the compensation paid to the said Miller during the calendar year 1940 was approved and ratified at the annual meeting of the shareholders on January 21, 1941, only over and against the objection and protest of the plaintiff herein. There was substantial and ample evidence to support such a finding and there was no evidence to the contrary.

30. The District Court erred in not finding that the compensation paid to the said Miller from January 1, 1941 to September 10, 1941, was approved and ratified at the annual meeting of the shareholders on January 20, 1942, only over and against the objection and protest of the plaintiff herein. There was substantial and ample evidence to support such a finding and there was no evidence to the contrary.

31. The District Court erred in finding that the resolutions of stockholders or any part thereof mentioned in paragraphs 29 and 30 hereof were regularly and/or legally adopted or adopted in good faith and/or without fraud by each and all or any of the stock-

holders voting for the same. There was no evidence to support this finding. The evidence was to the contrary.

32. The District Court erred in not finding that the amount of the salaries and compensation of the said Ballagh and the said Miller were fixed with the purpose and intent of depriving the plaintiff of dividends accruing or to accrue to plaintiff from the said Patterson-Ballagh Corporation. There was substantial and ample evidence to support such a finding and there was no evidence to the contrary.

33. The District Court erred in not finding that, if said excessive salaries and compensation had not been paid to the said Ballagh and the said Miller, such excess would have been available for the payment of dividends to the stockholders of Patterson-Ballagh Corporation, including the plaintiff. There was substantial and ample evidence to support such a finding and there was no evidence to the contrary.

34. The District Court erred in not finding that the amount of the salaries and compensation to the said Ballagh and the said Miller were neither fairly nor honestly determined by the said Ballagh and the said Miller. There was substantial and ample evidence to support such a finding and there was no evidence to the contrary.

35. The District Court erred in not finding that for and on account of the payment of excessive salaries and compensation the defendants Ballagh and Miller are indebted to said Patterson-Ballagh Corporation in at least the sum of $41,416.66, no part of

which has been repaid by the said Ballagh and the said Miller, or either thereof, to the said corporation. There was substantial and ample evidence to support such a finding and there was no evidence to the contrary.

36. The District Court erred in not finding that plaintiff failed to obtain any action by the directors or the stockholders of Patterson-Ballagh Corporation due to the domination, control, and direction of said corporation by the said Ballagh and the said Miller, and due to a scheme and conspiracy to defraud, entered into by the said Ballagh and the said Miller. There was substantial and ample evidence to support such a finding and there was no evidence to the contrary.

37. The District Court erred in finding that, prior to the participation in and approving of the election of H. C. Armisted, Howard Burrell, J. C. Ballagh and D. G. Miller as directors and officers on June 21, 1941, the said Dulin knew the attitude of said persons concerning the compensation that said persons considered should properly be paid to the said Ballagh and the said Miller during 1941. There was no evidence to support this finding. The evidence was to the contrary.

38. The District Court erred in finding that plaintiff has waived any right it might have to complain of the compensation paid to the said Ballagh and/or the said Miller by Patterson-Ballagh Corporation from January 1, 1941, to the time of filing suit herein on

September 10, 1941. There was no evidence to support this finding. The evidence was to the contrary.

39. The District Court erred in concluding, as a conclusion of law, that the compensation paid by Patterson-Ballagh Corporation to the said Ballagh from January 1, 1939 to the time of filing suit herein has been fair, just, or reasonable as to said corporation at the various times it was authorized, approved, or paid. There was no evidence to support any such conclusion. The evidence was to the contrary. The conclusion was erroneous as a matter of law.

40. The District Court erred in concluding, as a conclusion of law, that the compensation paid by Patterson-Ballagh Corporation to the said Miller from January 1, 1940 to the time of filing suit herein was fair, just, or reasonable as to said corporation at the various times it was authorized, approved, or paid. There was no evidence to support any such conclusion. The evidence was to the contrary. The conclusion was erroneous as a matter of law.

41. The District Court erred in concluding, as a conclusion of law, that plaintiff has waived any right to complain of the compensation paid by Patterson-Ballagh Corporation to the said Ballagh and/or the said Miller from January 1, 1940 to the time of filing suit herein. There was no evidence to support any such conclusion. The evidence was to the contrary. The conclusion was erroneous as a matter of law.

42. The District Court erred in concluding, as a conclusion of law, that plaintiff has waived any right

to complain of the compensation paid by Patterson-Ballagh Corporation to the said Ballagh and the said Miller from January 1, 1941 to the time of filing suit herein on September 10, 1941. There was no evidence to support any such conclusion. The evidence was to the contrary. The conclusion was erroneous as a matter of law.

43. The District Court erred in finding and concluding that plaintiff is not entitled either on its own behalf or on behalf of Patterson-Ballagh Corporation to any relief or recovery whatsoever against any of said defendants. There was no evidence to support any such finding or conclusion. The evidence was to the contrary. The conclusion was erroneous as a matter of law.

44. The District Court erred in finding and concluding that the defendants herein, or any of said defendants, are entitled to recovery of or from plaintiff their, his, or its respective costs of suit herein incurred. There was no evidence to support any such finding or conclusion. The evidence was to the contrary. The conclusion was erroneous as a matter of law.

45. The District Court erred in ordering that judgment be entered in favor of the defendants. There was no evidence and there were no findings, except erroneous findings, to support this order.

46. If the District Court, in determining the value of the services of the said Ballagh to Patterson-Ballagh Corporation, or in determining that the salary

and/or compensation of the said Ballagh for services to Patterson-Ballagh Corporation was not excessive, took into consideration the value of any claimed services rendered by him as an inventor or as the patentee of any inventions or as the applicant for any patent or the value of any inventions or of any patents or of any applications for patents of the said Ballagh, whether or not assigned to Patterson-Ballagh Corporation, the said District Court erred in so doing. Such claimed services were not rendered to Patterson-Ballagh Corporation and, if rendered, were outside of the scope of Ballagh's employment by such corporation.

47. If the District Court, in determining the value of the services of the said Miller to Patterson-Ballagh Corporation, or in determining that the salary and/or compensation of the said Miller for services to Patterson-Ballagh Corporation was not excessive, took into consideration the value of any claimed services rendered by him as an inventor or as the patentee of any inventions or as the applicant for any patent or the value of any inventions or of any patents or of any applications for patents of the said Miller, whether or not assigned to Patterson-Ballagh Corporation, the said District Court erred in so doing. Such claimed services were not rendered to Patterson-Ballagh Corporation and, if rendered, were outside of the scope of Miller's employment by such corporation.

SUMMARY OF APPELLANT'S ARGUMENT.

There is only one real issue in this case, to wit, were the salaries of the defendants Ballagh and Miller (during the years 1939 and 1940 and that part of the year 1941 prior to September 10, the date of the commencement of this action) excessive?[4] Appellant's argument that they were excessive divides itself as follows:

1. Due to the relationship of the defendants to the Corporation it was not only unnecessary for plaintiff to establish fraud, but a presumption arose in plaintiff's favor that the salaries were excessive.

2. The following circumstances establish the excessiveness of the salaries. These circumstances, when considered together, are conclusive:

(a) The salaries paid to the defendants were vastly in excess of salaries paid by comparable and even by much larger companies.

(b) The salaries paid to the defendants were several times greater than their prior compensa-

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[4]The expression "only real issue in this case" is used advisedly. By an amendment to the answer presented at the trial, the defendants for the first time set up a claimed waiver by plaintiff of its right to insist upon a return to the Corporation of any part of defendants' salaries (R., 29). Later defendants limited their claim to a waiver for the period subsequent to January 1, 1941, and the Court erroneously found that for such limited period the defense of waiver was good (R., 69-72). The defense was obviously an afterthought and was in direct conflict with uncontradicted testimony in the record that all salaries as to which complaint is made by plaintiff were fixed by the defendants over plaintiff's express objections (R., 243-244; 265; 298-306). Unless counsel have something to urge in addition to what was urged in the trial Court, our statement that there is "only one real issue" is unqualifiedly true. We await defendants' brief.

tion from other companies by which they had been employed.

(c) The salaries paid to the defendants were out of all proportion to the net profits of the Corporation.

(d) The salaries paid to the defendants were out of all proportion to the invested capital and the size of the business of the Corporation.

(e) The increases in defendants' salaries were made without any corresponding increase in the amount or the responsibility of the services rendered or to be rendered by them.

3. The defendants' salaries were not justified, in whole or in part, by defendants' claimed services as inventors.

(a) The By-Laws of the Corporation and the resolutions passed by its Board of Directors showed that the defendants were not being compensated as inventors.

(b) Any services as inventors were not performed for the Corporation.

(c) The inventions of the defendants could not be classed as services.

(d) Even if the inventions of the defendants are considered, they were not of sufficient value to support the amount of the salaries.

4. Defendants' salaries were part of a conspiracy by defendants to fraudulently enrich themselves at the expense of plaintiff, the minority stockholder.

CONCISE ARGUMENT OF THE CASE.

1.

DUE TO THE RELATIONSHIP OF THE DEFENDANTS TO THE CORPORATION IT WAS NOT ONLY UNNECESSARY FOR PLAINTIFF TO ESTABLISH FRAUD, BUT A PRESUMPTION AROSE IN PLAINTIFF'S FAVOR THAT THE SALARIES WERE EXCESSIVE.

During the period in question the defendants were the beneficial owners of seven hundred and fifty (750) of the outstanding one thousand (1,000) shares of the Corporation (R., 61). The Board of Directors consisted of five members, all of whom, with the exception of Dulin (plaintiff's President) had been selected by the defendants (R., 352-354; 391; 393). Miller was President and General Manager, Ballagh was Secretary and Treasurer and Sales Manager (R., 62). The other directors were Burrell and Armington. They never voted against the defendants and took little part in the meetings (R., 394; 449; 537). The defendants absolutely directed the acts and policies of the Corporation (R., 354; 381; 399). Dulin was never consulted as to the amount of salaries (R., 355-357; 392). The amounts were fixed in advance by Ballagh and Miller (R., 355-357; 361; 381; 384; 390). Dulin was always protesting (R., 243-244; 265; 298-306). In one case salaries were raised by Ballagh and Miller without even the formality of a directors' meeting (R., 355).

The foregoing facts show conclusively that the defendants fixed their own salaries. They were dealing with themselves. When directors of a corporation are in this position, a minority stockholder, in order to

force restitution by the directors to the corporation, need not establish fraud; there, also, arises a presumption that the salaries were unreasonable and the burden of proof is upon the directors to show the contrary. *Stratis v. Andreson,* 254 Mass. 536, 150 N. E. 832, and cited cases, should be conclusive. We quote from the *Stratis* case as follows:

> "It is immaterial in this connection whether there was actual fraud. The right of recovery for the benefit of the corporation rests upon the excessive payment to a director. Von Arnim v. American Tube Works, 74 N. E. 680, 188 Mass. 515; Meyer v. Ft. Hill Engraving Co., 143 N. E. 915, 249 Mass. 302. This conclusion is supported by the great weight of authority elsewhere. Carr v. Kimball, 139 N. Y. S. 253, 153 App. Div. 825, affirmed in 109 N. E. 1068, 215 N. Y. 634; Godley v. Crandall & Godley Co., 105 N. E. 818, 212 N. Y. 121, 130, 131, L. R. A. 1915D, 632; Decatur Mineral Land Co. v. Palm, 21 So. 315, 113 Ala. 531, 59 Am. St. Rep. 140; Beha v. Martin, 171 S. W. 393, 161 Ky. 838, 844; Matthews v. Headley Chocolate Co., 100 A. 645, 130 Md. 523, 536; Green v. National Advertising & Amusement Co., 162 N. W. 1056, 137 Minn. 65, L.R.A. 1917E, 784; Lillard v. Oil, Paint & Drug Co., 56 A. 254, 58 A. 188, 70 N. J. Eq. 197; Booth v. Beattie, 118 A. 257, 123 A. 925, 95 N. J. Eq. 776; Sotter v. Coatesville Boiler Works, 101 A. 744, 257 Pa. 411."

There is some very appropriate language in *Geddes v. Anaconda Mining Co.,* 254 U. S. 590. We quote from page 599 of the opinion:

"The relation of directors to corporations is of such a fiduciary nature that transactions between boards having common members are regarded as jealously by the law as are personal dealings between a director and his corporation, and where the fairness of such transactions is challenged the burden is upon those who would maintain them to show their entire fairness and where a sale is involved the full adequacy of the consideration. Especially is this true where a common director is dominating in influence or in character. This court has been consistently emphatic in the application of this rule, which, it has declared, is founded in soundest morality, and we now add in the soundest business policy. *Twin-Luck Oil Co. v. Marbury,* 91 U. S. 587, 588; *Thomas v. Brownville Ft. Kearney & Pacific R. R. Co.,* 109 U. S. 522; *Wardell v. Railroad Co.,* 103 U. S. 651, 658; *Corsicana National Bank v. Johnson,* 251 U. S. 68, 90." (Underscoring ours.)

Although *Davids v. Davids,* 120 N. Y. Sup. 350, is a holding by an inferior court, nevertheless the language is so well chosen that we quote from page 353, as follows:

"It is also urged on the part of the appellants that the plaintiff failed to prove the salaries voted were excessive, and that the bad faith of the directors cannot be presumed. The suggestion is based upon an erroneous assumption as to the precise relation in which the defendants, as directors, stood to the corporation. They occupied a position of trust, and, when the fact appeared that they had voted themselves salaries by a resolution in which they all joined, then they were

> put in the position of trustees dealing with themselves, to their own advantage, with respect to their trust. In such case the presumption is that they acted in their own interest, to the prejudice of the corporation, and the burden was upon them to overcome such presumption. Sage v. Culver, 147 N. Y. 241, 41 N. E. 513."

Authorities to the same effect are: *Schall v. Althaus,* 203 N. Y. S. 36; *Carr v. Kimball,* 139 N. Y. S. 253; *Ross v. Quinnesec Iron Mining Co.,* 227 Fed. 337; *Church v. Harnit,* 35 Fed. (2d) 499; *Jordan v. Jordan Co.,* 94 Conn. 384, 109 Atl. 181; *O'Leary v. Seemann,* 76 Colo. 335, 232 Pac. 667; *Davis v. Thomas A. Davis Co.,* 63 N. J. Eq. 572, 52 Atl. 717, p. 718.

At this point, and before proceeding with the following argument, we desire to make it clear that plaintiff is confident the court will not be called upon to rely upon the foregoing authorities. These authorities emphasize the position in which the defendants find themselves and, if necessary, plaintiff would be justified in urging a reversal based thereon. It will be demonstrated that there is no necessity for urging the presumption in favor of plaintiff. The amounts of the salaries themselves, in light of the circumstances in this case, are conclusive as to their excessiveness. It will, furthermore, be demonstrated at the end of this brief that the defendants in drawing their salaries were guilty of fraud. As a matter of fact, there is only one phase of this case where the foregoing principles may, if at all, become material (pages 42 to 47 hereof).

2.

THE CIRCUMSTANCES ESTABLISHING THE EXCESSIVENESS OF DEFENDANTS' SALARIES ARE SEVERAL. TAKEN TOGETHER THEY ARE CONCLUSIVE.

We again set forth the amounts of those salaries:

	For the calendar year 1939	For the calendar year 1940	For that portion of the calendar year 1941 prior to September 10
Ballagh	$15,000.00	$30,166.66	$19,000.00[6]
Miller	13,000.00[5]	19,750.00	12,000.00[6]
Totals for the two executives (R., 66.)	$28,000.00	$49,916.66	$31,000.00

(a) The salaries paid to the defendants were vastly in excess of salaries paid by comparable and even by much larger companies.

Through the witness Bunch there was put in evidence a long list of companies showing the total of their two highest executive salaries, the amounts of their capital and surplus, and their profit or loss figures. This tabulation (Ex. 19, R., 438) is instructive. We set it forth at length:

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[5]The above item of $13,000 paid to Miller in 1939 was not included in plaintiff's complaint. The setting forth of this figure is purely informative.

[6]These figures do not give an accurate picture, since the defendants had been taking from the Corporation additional amounts toward the close of each year. In the fiscal year 1941 their combined salaries were $53,666.00 (Ex. 5C).

Fiscal Year		Two Highest Salaries	Capital and Surplus	Profit or Loss
12/31/41	Gladding McBean & Co.	$49,673	$7,447,062	$ 603,984
12/31/40	Western Pipe & Steel Co. of Cal.	45,200	4,576,212	312,477
6/30/40	Hancock Oil Co. of Calif.	44,150	4,613,811	1,138,528
8/31/41	Consolidated Steel Corp.	44,000	4,841,381	667,518
12/31/40	Sontag Chain Stores Co.	40,120	2,128,971	225,931
12/31/40	Lane Wells Co.	38,500	2,206,900	605,977
12/31/40	Emsco Derrick & Equipment Co.	38,400	3,687,015	*82,475
12/31/40	Ryan Aeronautical Co.	37,688	1,424,821	358,344
12/29/40	Van de Kamp's Holland Dutch Bakers	37,100	1,204,215	203,209
12/31/40	Los Angeles Investment Co.	32,950	6,262,240	161,474
12/31/40	Puget Sound Pulp & Timber Co.	31,600	5,034,611	795,553
12/31/40	Blue Diamond Corp.	30,060	2,201,131	55,935
12/31/40	Electrical Products Corp.	28,578	2,120,478	342,674
12/31/40	Universal Consolidated Oil Co.	24,530	1,612,734	228,190
12/31/40	General Metals Corp.	21,200	1,216,189	259,623
12/31/40	Pacific Clay Products Co.	21,037	1,454,661	53,236
12/31/40	Taylor Milling Co.	21,000	2,421,223	197,589
12/31/40	Bolsa Chica Oil Corp.	15,675	1,034,417	*47,907*
12/31/40	Weber Showcase & Fixture Co.	14,822	2,060,724	58,692
5/27/40	Solar Aircraft Co.	14,034	747,819	51,546
6/30/40	Menasco Manufacturing Co.	14,000	873,021	190,137
6/30/40	Roberts Public Markets, Inc.	13,000	631,205	206,252
12/31/40	Bandini Petroleum Co.	10,680	1,538,075	2,412
12/31/40	Holly Development Co.	9,650	721,569	51,691
12/31/40	Merchants Petroleum Co.	9,400	167,904	*2,082*
10/31/40	Intercoast Petroleum Co.	8,600	428,668	3,080
12/31/40	Lincoln Petroleum Co.	8,020	143,369	*27,613*
12/31/40	Oceanic Oil Co.	6,650	256,502	*6,565*
12/31/40	Norden Corp., Ltd.	5,935	377,153	10,793
12/31/40	Mascot Oil Co.	5,400	329,492	4,789
12/31/40	Rice Ranch Oil Co.	5,013	284,502	12,089
12/31/40	Occidental Petroleum Co.	4,895	140,785	*418*
12/31/40	Holly Oil Co.	4,800	399,505	*10,092*
2/28/41	Mount Diablo Oil, Mining & Development Co.	3,950	139,201	13,874
12/30/41	Patterson-Ballagh Corp.	53,666	201,023	22,999

*Italics designate losses.

It will thus be seen from the foregoing tabulation that not one of the listed companies paid compensation as large as this corporation, and that the only companies paying compensation which even approached the compensation paid to the two defendants were organizations with a capital and surplus of better than $2,000,000 and, in one case, over $7,000,000, with yearly profits ranging from $225,000 to over $1,100,000. The capital and surplus of Patterson-Ballagh Corporation at best, was only a little over $200,000 (Ex. 5C). The Corporation's net profits (after the deduction of salaries, as was the case with the Bunch figures) for the fiscal year 1938 were $26,496.35; for the fiscal year 1939, $20,927.25; for the fiscal year 1940, $20,519.85; and for the fiscal year 1941, $19,220.64 (Ex. 5). The fiscal year of this Corporation ended upon November 30. Any variations between the calendar and fiscal year are of no great importance.

(b) The salaries paid to the defendants were several times greater than their prior compensation had been from other companies by which they had been employed.

The record shows without conflict that, in prior employment, the defendant Miller had earned not in excess of $800 per month and, likewise, the defendant Ballagh not in excess of $800 per month (R., 379; 539). Although plaintiff concedes that the amounts of salaries which had been paid by other concerns to the defendants are not conclusive, these amounts are certainly not only instructive, but most persuasive, when such vast discrepancies as in the present case are shown.

(c) The salaries paid to the defendants were out of all proportion to the net profits of the Corporation.

The Corporation's net profits before deduction of the defendants' salaries were, for the year 1939, $48,927,[7] for the year 1940, $68,936, and for the year 1941, $72,887. The combined salaries of defendants for the year 1939 were $28,000, for the year 1940, $48,417, and for the year 1941, $53,666. These figures show that defendants were taking the following percentages out of net profits (before the deduction of their salaries), to-wit: For the year 1939—57%, for the year 1940—70%, and for the year 1941—74%. This all appears on Exhibit 18A.

It is interesting to note that although the profits did increase somewhat during these years, the increase in salaries was infinitely greater in proportion and that profits apparently furnished no yardstick.

The earnings of the Corporation, about the times of the respective raises, should be considered.

The first raise was upon August 22, 1939, retroactive to March 1st (R., 230). According to the Corporation's own statements the Corporation sustained a loss in August of $1,814.59. Its profit for July had only been $1,940.11, for June $3,871.13, and for May $1,-865.67. At that time, and for the period since November 30, 1938, it was in the "red" $2,408.94. In April it had sustained a loss of $645.78 (Ex. 6A). This was no time for a raise. The Corporation's own statements were not, however, accurate. Conditions were

[7]This and the following figures refer to fiscal years.

much worse. Those statements showed, for the year 1939, a profit of $33,978.44. When Messrs. Pennington-Swanson, the certified public accountants, examined the profits for the year, the figure of $33,978.44 was reduced to $20,927.25 (Ex. 5A).

The second raise of salaries occurred on March 18, 1940 (R., 242-243). The Corporation's figures showed a profit for March in the sum of $10,485.50, for February of $11,663.33, for January of $7,567.04, and for December, 1939, of $5,375.62. These figures were, again, not accurate. The Corporation placed its net profit for the fiscal year 1940 at $51,586.70 (Ex. 6B). Messrs. Pennington-Swanson arrived at the figure of $20,-519.85 (Ex. 5B). Furthermore, the outlook in March of 1940 for future profits was not good. Profits, except for one month, namely, the month of July, when they were $10,643.00, showed a marked decrease. In May they were only $2,883.67; in June $2,887.53; in August $4,033.64; in September $3,211.79, and in October $1,676.07. In November we meet a loss of $11,-178.34 (Ex. 6B). Again this was no time for a raise.

The next raise was on November 29, 1940 (R., 251-252). The figures already given demonstrate that it was no time for a raise.

Of interest also are the profits for 1941. The Corporation's own figures place them at $35,722.73 (Ex. 6C). Messrs. Pennington-Swanson decreased this figure to $19,220.64 (Ex. 5C). Notwithstanding, the salaries to the defendants were not reduced but continued at the same rate.

We refer again to the Bunch figures. His profit and loss figures are, however, after deduction of the salaries of the two highest executives. They present no cases at all comparable, except cases where at least one of the two following elements was present, to-wit: either the particular company was operating at a loss, or the particular company had several times more capital and surplus invested. Even in each one of those exceptional cases the total, in dollars and cents, of the two highest salaries was less than in the present case.

(d) Salaries paid to the defendants were out of all proportion to the invested capital and the size of the business of the Corporation.

The capital and surplus of the Corporation during the period involved in this litigation was, at best, only a little over $200,000 (Ex. 5-C).[8] If the figures of the witness Bunch are again taken for comparison, we find that the compensation of the defendants was out of all reason. Those figures show that in a company with capital and surplus of the size of this Corporation the combined salaries of the two highest paid executives should run at most between $9,000 and $10,000 per annum. The defendants' salaries for the fiscal

[8]The Corporations' own financial statements, as well as the Pennington-Swanson statements, gave a figure for capital and surplus for the years 1939-1940 considerably larger than for 1941. This was due to the fact that in those years an item in the amount of $80,703.61 for good will appeared. This item of good will was thrown out the window in 1941 and, therefore, bears all the earmarks of having been "water". Eliminating good will, the exact figures for capital and surplus, as shown by the certified accountants, were, for 1939, $162,894.81; for 1940, $181,802.80, and for 1941, $201,023.44 (Ex. 5).

year 1940 were $48,417, and $53,666 for the fiscal year 1941 (Ex. 18-A).

Certain aspects of the Corporation's business may at this point be material. The Corporation had only one manufacturing establishment, which was small (R., 349-350; 555); the average number of its employees, in all parts of the country, was probably only about forty (R., 350); the Corporation had no financial problems which would require exceptional services (R., 350); the business could be well classed as a small "specialty business". There are hundreds of such businesses in southern California and elsewhere. It would be a matter of amazement if any one of them presented such a salary picture.

The witness Bunch labored under a handicap. He could not delve into the financial matters of these numerous businesses. He was forced to confine himself to companies whose finances were public property. Nevertheless, the Bunch figures certainly demonstrate enough. Salaries for the two highest executives of $50,000 per annum, more or less, must be out of all proportion to a capital and surplus of approximately $200,000. They reached the annual rate of over one-fourth of the entire capital and surplus.

(e) The increases in defendants' salaries were made without any corresponding increase in the amount of the responsibility of the services rendered or to be rendered by defendants.

Ballagh's salary was increased from $15,500 in the fiscal year 1939 to almost $30,000 in the fiscal year 1940 (R. 277-282). Miller's salary was increased from

$13,000 in 1939 to almost $20,000 in 1940. Their combined salaries amounted to $53,666 in 1941 (Ex. 18-A). We ask, "How can these increases be justified?"

There were no corresponding increases either in the duties or responsibility of Ballagh (R., 350-351). Miller took over the exact same work as Patterson had been doing. There was no increase in Miller's duties or responsibilities (R., 351; 381).

It is well established law that ordinarily there should be an increase in duties or responsibilities in order to warrant an increase in salaries. We cite *Schall v. Althaus,* 203 N. Y. S. 36; *Atwater v. Elkhorn Valley Coal Land Co.,* 171 N. Y. S. 552; *Kreitner v. Burgweger,* 160 N. Y. S. 256; *Raynolds v. Diamond Mills Paper Co.,* 69 N. J. Eq. 299, 60 Atl. 941, pp. 947, 948.

In the *Raynolds* case, after mentioning the lack of increase in services rendered, the court said:

> ". . . . I incline to think that this is an instance where equity should look behind the fiction of corporate existence, and, in measuring the compensation of the managers of a corporation by the success which their operations have attained, analyze the success to a large extent, if not wholly, from the stockholder's point of view—from the point of view of the man who cannot touch a dollar of the accumulated profits of the corporation until a dividend has been declared."

It is again of note that during the period of importance in this case the Corporation never declared a dividend in which plaintiff could share, and ceased

to pay royalties to the plaintiff, which the Corporation had contracted to pay by the terms of the agreements introduced as Exhibits 15-A, 15-B, 15-C, 15-D. We mention this in passing.

3.

THE DEFENDANTS' SALARIES CANNOT BE JUSTIFIED, IN WHOLE OR IN PART, BY DEFENDANTS' CLAIMED SERVICES AS INVENTORS.

In approaching this subject, it is well to dwell for a moment upon the injustice of allowing the defendants to prevail by relying upon their claimed inventions. The complaint in this case was drawn upon the theory that there should be paid back to the corporation the excessive parts of the salaries paid to the individual defendants as President and Secretary and Treasurer. Not one word was said about inventions or patents. The answer was in due course filed. There was no word of inventions or patents. It was not until the trial that this element developed. Plaintiff was given no notice that the value of patent rights or inventions would be in any manner involved. These rights or inventions had never been put into issue and, therefore, in all fairness, should not have been considered by the Court.

If the individual defendants had any rights against the Corporation in regard to their inventions or patents, which they claim to have transferred to the Corporation, they should have brought a separate suit or perhaps have interposed a counterclaim or cross-

complaint. Neither course was taken. The obvious conclusion is that counsel, finding impossibility in justifying the salaries of the two gentlemen as president and secretary and treasurer, resorted to this other element in hopes of success. If counsel is at liberty to do so, there is no reason why, when a corporate officer is sued for excessive salaries received as such officer, he should not be at liberty to drag out of the dim and distant past some claimed benefit in the conveyance of property, use of personal influence, lobbying, or whatnot, and thus try to justify what he has received.

(a) The By-Laws of the Corporation and the resolutions passed by its Board of Directors showed that the defendants were not being compensated as inventors.

Section 3 of Article III of the By-Laws reads as follows: "The officers may receive only such salaries as the Board of Directors may from time to time determine. Until the salary of an officer has been fixed by resolution of the Board of Directors, such officer shall serve without compensation." (R., 108.)

This By-Law provided, in effect, that unless the salary of an officer had been fixed by resolution such officer was to serve without compensation.

The resolutions of the Directors as to the salaries should be read. They show expressly that Miller was being compensated as President and General Manager and in no other capacity; they show that Ballagh was being compensated as Secretary and Treasurer and Sales Manager and in no other capacity. They were not being compensated as inventors. The minutes do

not even casually mention any such employment. We consider this element of such importance that we quote from the minutes at length and set forth the pertinent excerpts in the Appendix to this brief.

Furthermore, inventions were never mentioned as a reason for increase of salaries (R., 395-396).

Defendants are attempting to justify compensation paid them in specified capacities by resorting to claims that they should have received compensation in other capacities. The case of *Stratis v. Andreson,* 254 Mass. 536, 150 N. E. 832, is in point. There the salary of the Treasurer, General Manager, and Clerk, who were one and the same person, was not paid as a single item, but was divided into three separate items. The Supreme Judicial Court of Massachusetts held that each separate item must stand on its own footing. The following appears in the opinion:

> "The salary to the treasurer, general manager and clerk was not a single item but was divided into three separate items. Each item must stand on its own footing. The salary paid him as clerk has been found to be more than its fair value and the excess must be returned even though the entire compensation regarded as a unit was not excessive. It was not paid as a unit."

Lillard v. Oil, Paint & Drug Co., 70 N. J. Eq. 197, 56 Atl. 254, contains a somewhat similar situation. There the manager of a corporation, in an attempt to justify his salary, which was greatly in excess of the salary of his predecessor, showed that his predecessor was receiving other benefits from the corporation

which should be taken into consideration. The court held no, and said, at page 260:

> "The argument that the payment of dividends to Lillard was really a salary, and, together with his salary, amounted to much more than Allison received as salary, and the latter's salary is therefore to be considered fair, is also unsound. This transaction was a purchase for which Lillard gave his notes to Allison and became his debtor. He owned, before the purchase, a large number of shares, and the transaction as between Allison and Lillard was in all respects a purchase of the stock, and not an arrangement for salary. It was so considered and treated by both, and, although the business under Lillard's management was so profitable as to pay the notes for the purchase largely out of his dividends on the stock purchased, Lillard took the risk, when he gave the notes, that they might not be paid out of the profits, and Allison derived his proportionate benefits as stockholder by the dividends received on his stock under Lillard's management. The payment of Lillard's notes from this source is not now to be considered as a salary, or as justifying Allison's sure return, in the form of a large salary for management, of a sum approximating or proportioned to the dividends Lillard received on his stock while manager."

Again referring to the *Stratis case,* it is self-evident that, if overpayment to an officer in one capacity cannot be justified by underpayment to the same person acting in another capacity, certainly an overpayment as president or secretary and treasurer or manager or sales manager cannot be justified by claimed com-

pensation which was never authorized in any corporate resolution.

It was conceded by counsel in the trial court that the defendants must look to the resolutions of the Board of Directors for such compensation as they received. There was no mention of inventions in any of the resolutions. At page 23 of their brief on motion for a new trial, the following appeared:

> "However, at this point, an important distinction between the cases cited by plaintiff and the position of defendants herein must be borne in mind. The individual defendants in this case are not seeking to recover compensation which has never been authorized. They are seeking merely to retain compensation paid to them pursuant to duly authorized resolutions." (Underscoring ours.)

(b) The services as inventors, for which the defendants claim compensation, were never performed for the Corporation.

These services were performed by the individual defendants for themselves. This was conceded by counsel in the trial court. On page 40 of their brief on motion for a new trial, the following appeared:

> "As to the law on the patents existing in this case and on those patents anticipated as the result of the inventions involved in this case, it is certain that prior to the assignments of such patent or patent applications, title to the patents or patent rights was in the individual defendants."

Counsel's position finds the following uncontradicted support in the record:

"By Mr. Bednar. Q. Mr. Ballagh, has there ever been any contract between you and Patterson-Ballagh Corporation requiring you to spend your time inventing?

A. No, sir.

Q. Has there ever been any such contract as to Mr. Miller?

A. No, sir.

Q. Has there ever been any contract between you and Patterson-Ballagh Corporation requiring you to assign any of your inventive rights or patents to the corporation?

A. No, sir.

Q. Has there ever been any such contract as to Mr. Miller?

A. No, sir." (Ballagh's Testimony, R., 506.)

"Q. At any of these meetings of the Patterson-Ballagh Company which you attended, was anything ever said as to employing either Mr. Ballagh or Mr. Miller as inventors or designers?

A. Never." (Dulin's Testimony, R., 393.)

"Q. When these inventions were originally made, whom did they belong to?

A. Ballagh.

Q. And is it your position that until they were transferred to the company they still belonged to Ballagh?

A. Yes. Mr. Patterson, for example, had made a patent some four or five years previously, which he took in his own name and refused to recognize the company as having any interest in it of any character." (Burrell's Testimony, (the Corporation's attorney), R., 450.)

Thus it is apparent that even considering patents or inventions in the category of services rendered, they were not rendered to the Corporation.

There is evidence that the two defendants had assigned, or would assign, their inventions to the Corporation. There was never any action, however, by the board of directors authorizing the purchase of these inventions. In fact, the inventions and the assignments were unknown to plaintiff (R., 406). At best, what happened was that certain assignments may have been made, but, if so, they were voluntarily made, due no doubt to the fact that the two defendants owned three-fourths of the stock, and were treating the Corporation as their own. They did not for a moment believe that plaintiff could profit by any such transfer. They had no intention of paying further dividends or royalties. They knew that the payment of dividends could not be forced, and they had secured an opinion of counsel that royalties could be forgotten (R., 225). No inventive services were ever rendered to the Corporation. As heretofore pointed out, the evidence was, without qualification, to the contrary.

Authorities are to the effect that when an officer performs services outside of his duties he must have a contract with the Corporation before he can recover for such services. We cite *Finch v. Warrior Cement Corporation,* 16 Del. Ch. 44, 141 Atl. 54; *Jones v. Foster,* 70 Fed. (2d) 200; *O'Leary v. Seemann,* 76 Colo. 335, 232 Pac. 667; *Pindell v. Conlon Corporation,* 303 Ill. App. 232, 24 N. E. (2d) 882; *Larkin v. Enright,* 312 Ill. App. 184, 37 N. E. (2d) 905; ***In re Dr. Voorhees Awning Hood Co.,*** **187 Fed. 611.**

(c) The inventions of the defendants cannot be classified as services.

We are not dealing with services, but with property rights. The defendants were at liberty to transfer or not to transfer these property rights as they saw fit. Their duties as President or General Manager, or Secretary or Treasurer or Sales Manager did not comprise inventive services (R., 373). Nowhere in the minutes is there mentioned any offer to transfer inventions, nor any acceptance of any such offer by the Corporation; in fact, the minutes make no reference to inventions. Had the Corporation suddenly become insolvent and creditors appeared at the front door, the patents and other rights heretofore transferred would never have been transferred and no additional transfers would have been made. This case results in a situation just as clear as though the defendants were attempting to bolster up excessive salaries by claiming that certain real estate or personal property, other than patents, transferred or to be transferred to the Corporation, should justify their salaries. Let us consider the reverse: Let us assume that the defendants had transferred a plant to the Corporation at a figure so excessive that it could not be justified. Let us assume that they were haled into court by a minority stockholder asking that the transaction be rescinded. Could they justify the excessive price by claiming that they were underpaid as officers, and that part of the money received as the purchase price was in fact additional salary? We cannot conceive of a court going this far. The same legal principles govern.

Counsel attempted to argue that when the Corporation accepted assignments of the inventions and proceeded to use them, the Corporation accepted the inventive services and impliedly agreed to pay therefor. This was the only explanation offered. The Board of Directors never accepted the assignments. Furthermore, with what are we dealing? Services or property? It cannot be both. Counsel conceded that the inventions belonged to the individual defendants up to the time of assignment. As pointed out, if creditors appeared they never would have been assigned, and the services would have remained services rendered by the defendants to themselves. This looks like property rights, and not services rendered to the Corporation. It is a novel doctrine of law that, if work is done in perfecting patents and those rights or patents are later transferred, the services in perfecting the patents immediately attach to the transferee and have been, *ex post facto,* rendered to such transferee. Counsel must have in mind some such doctrine as covenants running with the land. The whole sum and substance of the matter is that we are dealing with property rights and not with services.

(d) Even if the inventions of the defendants should be considered, they were not of sufficient value to support the amount of the salaries.

We anticipate that counsel will urge that as to this phase of the case there was a conflict in testimony and, therefore, we are foreclosed by the findings of the trial court. We point out that not only is this an

equity case, but also that under Rule 52(a) of the Rules of Civil Procedure, where findings are made by the court without a jury, the Appellate Court is not limited to the mere question whether there is any substantial evidence to support the findings, but may set them aside if against the clear weight of evidence (*State Farm Mut. Automobile Ins. Co. v. Bonacci,* 111 Fed. Rep. (2d) 412).

In this same connection we refer the court to the authorities cited at pages 23 to 25 of this brief, that the burden of proof was upon the defendants. We emphasize that the defendants, in urging the value of inventions, are dealing with an intangible. Throughout the case they were never able to demonstrate what value, if any, should be attributed to this intangible. Therefore, they could not have met the burden of proof.

Coming to the evidence, we first refer the court to Exhibit A. That exhibit was prepared by the defendants. It shows that by far the great part of the Corporation's business was in the sale of casing protectors.[9] As a matter of fact, of the total gross sales of the Corporation for the year 1939 of approximately $336,500, the sales of casing protectors constituted almost $262,000; for the year 1940, out of gross sales of approximately $330,000, casing protector sales amounted to almost $234,000; and for the year 1941, out

[9]"Casing protectors" are to be distinguished from "tubing protectors". "Tubing protectors" were a very minor item (R., 453).

of gross sales of a little over $366,000, casing protector sales amounted to approximately $245,000 (R., 343). The casing protector business had existed ever since the formation of the Corporation; in fact, had been taken over from the original partnership of Patterson & Ballagh. The defendants claim, however, that by invention they had improved the old casing protector by placing at each end thereof a so-called "lip". This was but a trivial improvement (R., 367). Not only does the testimony of the witnesses Chesnut and Grant so state (R., 544-545), but an examination of Exhibit E will so demonstrate.

There is no showing that the Corporation's business would not have proceeded equally well without the claimed invention and, for that matter, no lip protectors were sold in the year 1939 (R., 366), yet the protector business for that year substantially exceeded the protector business for the year 1940 and also for the year 1941. The witness Burrell admitted that the lip protector did not increase the protector business (R., 454).

The defendants also relied upon the claimed invention of the pipe wipers. The sales of pipe wipers were relatively unimportant. In 1939, out of total gross sales of about $337,000, the sales of pipe wipers were only slightly in excess of $12,000; in 1940, out of a total sales of about $330,000, the pipe wipers sales amounted to only a little over $30,000; and in 1941, out of total sales of approximately $366,500, the pipe wipers sales amounted to less than $44,000 (Ex. A). The same situation existed as to pipe wipers that ex-

isted as to protectors—there was competition (R., 371-372).

The only other item of any moment whatsoever in total sales of the Corporation was wire line guides. These usually outranked pipe wipers (R., 345) but they were not of defendants' invention; in fact, royalties were being paid thereon to other parties (Ex. A) (R., 458).

The other items were trivial and to a great extent were the inventions of outside parties to whom royalties were being paid (R., 346-347; 553-555). The largest of these other items as to which invention was claimed by the defendants was tubing protectors. In 1939 their sales amounted to only a little over $3000; in 1940 to less than $9000; and in 1941 to less than $17,000 (Ex. A).

The defendants stressed the importance of the hydraulic applicator, which they claim to have invented. The hydraulic applicator was not an article for sale but was a contrivance for placing casing protectors upon the drill pipe. The defendants claimed that it was much superior to the old mechanism. However, they are met with the fact that no patent had ever been granted (R., 492). Competition exists (R., 505). They are also met with the difficulty of a total lack of showing that the Corporation's business would not have been just as great had the hydraulic applicator never come into being. A reference to Exhibit A will show not only, as heretofore stressed, that the business in casing protectors was bigger in 1939

than in either 1940 or 1941, but that in the installations in 1939, only 7% thereof were made by the hydraulic applicator.

The witness Chesnut testified, among other things, in regard to all of the inventions, as follows:

> "A. I would say that they are well described by the term 'run of the mill inventions.' They relate to minor improvements, and probably useful improvements in inventions or in devices made by a specialty manufacturer, which includes rubber products in the oil industry, and in any business we expect the manufacturer will improve his products from time to time and find other items which fit into his line, and I would say they are just average inventions, if they are inventions." (R., 570.)

The witness Grant, who was a disinterested party and whose testimony commences at page 542 of the record, testified that the lip protector had very little, if any, advantage over the ordinary protector.

It is most noteworthy that the profits of the business did not greatly increase (Ex., 5). Counsel's position must be and, as we understand it, was that had it not been for the use of the inventions the business would have decreased. Of course, this is mere conjecture and surmise, and should be so labeled.

Certain additional circumstances are worthy of comment. The part played by the claimed inventions of Miller in the Corporation's total sales is infinitesimal (R., 376-377). In 1939 his claimed inventions played no part whatsoever; in 1940 they could, at best, have accounted for only approximately $2600; and in 1941

for only approximately $6000 (Ex. A) (R., 373). Neither the inventions of Miller nor those of Ballagh were ever discussed or mentioned, except perhaps in a negligible fashion, at the meetings of the stockholders or directors of the Corporation. The minutes are absolutely silent on the subject (Ex. 1, R., 206-267). The financial statements of the Corporation not only place no value upon the claimed inventions, but they were not even listed as an asset. It is surprising that they could have been of such great moment.

There is, however, a very considerable amount of testimony having to do with claimed inventions. Its only danger from our standpoint is its bulk. Due to its bulk it can be misleading. When analyzed, it amounts to no more than we have heretofore set forth.

We repeat that the defendants, in an attempt to justify their excessive salaries, are relying upon an intangible. There is not one iota of evidence as to the extent that any of the Corporation's business was increased by the claimed inventions. The increase in profits was not at an unusual rate, yet the increases in salaries were at a most unusual rate (Ex. 18). In fact, the defendants' claim seems to be that the claimed inventions kept the Corporation's business from decreasing. If true, to what extent, we do not know.

With the record in this shape it cannot be seriously urged that the defendants have met the burden of proof. They certainly have not met the burden of proof to the extent of justifying outrageously excessive salaries. We repeat, the urging of the so-called inventions as a justification was an afterthought.

4.

DEFENDANTS' SALARIES WERE PART OF A CONSPIRACY ON THE PART OF DEFENDANTS TO FRAUDULENTLY ENRICH THEMSELVES AT THE EXPENSE OF PLAINTIFF, THE MINORITY STOCKHOLDER.

The *bete noir* of this entire picture was the defendant Miller. Prior to the entreé of Miller, and under the guidance of Ballagh and Patterson, the Corporation had been paying salaries to Ballagh and Patterson at least to the extent that the law would allow. In numerous instances, in excess thereof. Miller, as heretofore pointed out, brought about three changes each working to plaintiff's detriment, namely, (1) the nonpayment of dividends; (2) the repudiation of the Corporation's obligation to pay plaintiff royalties as required by contract; and (3) the increase of salaries. These three changes were inaugurated at or about the same time. They had an only too apparent result—they enriched the defendants at the expense of the minority stockholder. Previously, dividends were paid by the Corporation. We venture, they would have continued to be paid except for the appearance of Miller. Royalties had always been paid. Both plaintiff's dividends and royalties had been in substantial amounts (Ex. 18).

Plaintiff could not, and still cannot, force the Corporation to pay dividends. It can, however, force the Corporation to continue the payment of royalties. This it is doing. There is now being appealed to this Court a case wherein Byron Jackson Co. sued the Corporation (Patterson-Ballagh Corporation) and in which Mr. Judge Hollzer, in the trial court, decided that the

plaintiff herein was entitled to royalties, and a judgment for royalties has been rendered in favor of plaintiff. Plaintiff should likewise be able to force the defendants to restore to the Corporation salaries paid to themselves to the extent of their excessiveness. If the holding of this Court is to the contrary, defendants will be given *carte blanche* to continue to bleed the Corporation to their own advantage and plaintiff might just as well write off to profit and loss its entire investment in the Corporation.

The repayment of the excess of salaries would not be disastrous to the defendants. The Corporation would be the recipient and defendants own a three-quarter interest therein. Failure to make restitution, however, would be the end of plaintiff's investment.

The universal law is that it is unlawful to distribute corporate profits in the guise of compensation. (*Wellington Bull & Co. v. Morris,* 230 N. Y. S. 122; *Green v. Felton,* 42 Ind. App. 675, 84 N. E. 166; *Carr v. Kimball,* 139 N. Y. S. 253; *Stratis v. Andreson,* 254 Mass. 536, 150 N. E. 832; *Barrett v. Smith,* 185 Minn. 596, 242 N. W. 392, pp. 393, 394; *Backus v. Finkelstein,* 23 Fed. (2d) 531, pp. 535, 537.)

To what extent the conspiracy of the defendants has succeeded can be shown no better than by the following compilation of figures, having to do with fiscal years, appearing upon Exhibit 18-D.

Distribution of Corporate Payments Between Byron Jackson Co. and Patterson, Ballagh, and Miller.

	BYRON JACKSON CO.			PATTERSON, BALLAGH AND MILLER[10]			
ear	Dividends	Royalties	Total	Salaries	Dividends	Royalties	Total
28	$ 20,000	$ 7,793.00	$ 27,793.00	$ 16,857	$ 60,000	.....	$ 76,85
29	83,750	38,401.21	122,151.21	48,000	251,250	.....	299,25
30	13,750	22,204.88	35,954.88	45,750	41,250	.....	87,00
31		2,188.61	2,188.61	23,000		.....	23,00
32		1,502.50	1,502.50	3,750		$ 1,502.50[11]	5,25
33		1,642.12	1,642.12	3,375		1,642.12	5,01
34		3,216.89	3,216.89	12,000		3,216.89	15,21
35		3,809.76	3,809.76	13,500		3,809.76	17,30
36	1,500	5,657.68	7,157.68	32,500	4,500	5,657.68	42,65
37		5,890.20	5,890.20	27,000		5,890.20	32,89
38	1,500	5,759.27	7,259.27	25,000	4,500	5,759.27	35,25
39		3,340.49	3,340.49	28,000		3,340.49	31,34
40		.....	.....	48,417			48,41
41		.....	.....	53,667			53,66
otals	$120,500	$101,406.61	$221,906.61	$380,816	$361,500	$30,818.91	$773,1

It will be noted from the foregoing that in 1939 plaintiff received its last royalties (this was prior to July 1st). It will be noted that plaintiff received no dividends after 1938. It will be noted that in the years 1939, 1940, and 1941, the defendants took from the Corporation over $130,000,—this by way of salaries in which plaintiff could not share.

---

[10]It will be recalled that in the early part of 1939; to-wit, on February 15, Patterson resigned as a director and President of the corporation and Miller thereupon took his place. All salary thereafter paid to the President of the corporation was paid to Miller.

[11]The royalty payments in this column arose by virtue of Exhibit 15-C. That contract provided that after plaintiff had received in royalties $75,000 under Exhibit 15-A plaintiff would assign to Patterson and Ballagh a one-half interest in the patents covered by Exhibit 15-A and a one-half interest in said agreement. This was done.

The picture presented would be bad enough if we were dealing with salaries paid to others than directors. It is unpardonable when the fiduciary relationship of directors to a minority stockholder enters. To establish fraud against directors the same degree of proof is not required as in the case of a stranger. (29 *Cal. Law Rev.* p. 190; *Wright v. Heublein,* 238 Fed. 321, 324; *Sagalyn v. Meekins, Packard & Wheat,* 290 Mass. 434, 195 N. E. 769, 771.)

The defendants have ridden roughshod over plaintiff's rights, and have constituted themselves trustees for themselves alone, and not for the minority stockholder. Their bad faith can be no better shown than by two illustrations in the record. Ballagh testified that the defendants did not consider their cash on hand adequate to pay dividends (R., 361); nevertheless, they raised their own salaries and in so doing took into consideration the fact that they were not paying dividends (R., 358; 363; 382). On June 27, 1939, at the time the conspiracy was formed, and just prior to the first salary increase which was approved by the board of directors on August 22, 1939, and made retroactive to March 1st of that year (Ballagh in the meantime having been drawing the increase), Miller wrote a letter to the Corporation which contained the following language:

> "Since assuming office as President of Patterson-Ballagh Corporation I have taken upon myself the duty of studying various costs in connection with the conduct of this business. I find that for the first six months of 1939 the corporation will show a loss of some $2,000." (R., 223.)

If Miller was sincere in his belief as to the loss of $2,000, and if he was sincere in his further statement appearing in the record that in making raises he considered the financial state of the business of the Corporation (R., 382), it was certainly a fine time for a salary increase.

Dated, September 10, 1943.

Respectfully submitted,

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(Appendix Follows.)

Appendix.

Appendix

From the minutes of the meeting of directors held October 1, 1936:

> "Upon motion of Mr. Patterson, seconded by Mr. Ballagh, the following resolution was adopted:
>
> > RESOLVED: That the Board of Directors fix the salaries of C. L. Patterson, President, and J. C. Ballagh, Secretary-Treasurer, at $1250.00 each per month effective as of August 1, 1936, and $2,000.00 each per month effective as of September 1, 1936.
>
> "Mr. Patterson and Mr. Ballagh voted in the affirmative, and Mr. Dulin voted in the negative, on the foregoing Resolution.
>
> "Mr. Dulin stated that, in his opinion, the administrative costs were out of all proportion to the volume of business transacted by Patterson-Ballagh Corporation, Ltd." (R., 113.)

From the minutes of the meeting of stockholders held on January 29, 1937:

> "Upon motion duly made, seconded and carried, the following Resolution was unanimously adopted:
>
> > BE IT RESOLVED, that each and every act of the directors of this corporation, and of each of the officers of this corporation, as shown by the records of this corporation, with the exception of the officers' salaries, and also with the exception of any acts of the officers expressly

disapproved by the Board of Directors of this corporation, be and the same are hereby ratified, adopted, approved and confirmed, as and for the acts of this corporation.

"Upon motion duly made and seconded the following Resolution was adopted:

BE IT RESOLVED, that the salaries prevailing for the past year of the two executive officers are hereby approved.

"Mr. Patterson and Mr. Ballagh voted in the affirmative, and Mr. Dulin voted in the negative, on the foregoing resolution.

"Mr. Dulin stated that, in his opinion, from the preliminary financial statement rendered the company's financial condition has not allowed the administrative salaries being paid which, in his opinion, are excessive, and further, the dividends declared during the year should not have been paid. Taking into consideration the condition of the business, the volume of sales, as a director and a stockholder, he urged that the administrative salaries be adjusted downward and that no further dividends be paid until the company is in a greatly improved financial position." (R., 124.)

From the minutes of the meeting of directors held on October 13, 1938:

"The next matter before the meeting was the matter of the increase in the officers' salaries. A general discussion was had and it was moved by Mr. Dulin, seconded by Mr. Elliott, that the salary of Mr. C. L. Patterson, President, be in-

creased to $1500.00 per month, effective September 1, 1938. Motion unanimously carried. It was thereupon moved by Mr. Dulin, seconded by Mr. Elliott, that the salary of Mr. J. C. Ballagh, Secretary-Treasurer of the company, be increased to $1500.00 per month, effective September 1, 1938. Motion unanimously carried." (R., 182.)

From the minutes of the meeting of the directors held on January 27, 1939:

"On motion of Mr. Dulin, seconded by Mr. Ballagh, and unanimously passed, the following resolutions were adopted:

RESOLVED, that the officers' salaries, viz. Mr. Patterson and Mr. Ballagh, be each One Thousand ($1,000.00) Dollars per month, effective January 1, 1939." (R., 203.)

From the minutes of the meeting of the directors held on February 15, 1939:

"COMPENSATION
OF PRESIDENT

The meeting then proceeded with the matter of considering the compensation to be paid to the President for his services and the advisability of designating him as General Manager of the business and affairs of the corporation. The suggestion was made that such compensation be fixed in the same amount as had been paid the former President since the first of the current year.

"Thereupon, on motion of Director Ballagh, seconded by Director Dulin and unanimously carried, it was

RESOLVED, that the President of this corporation shall be the General Manager of its business and affairs and that he shall receive as compensation for his services commencing as of February 15, 1939, the sum of $1,000.00 a month, payable in the same manner and on the same dates as other executive salaries." (R., 213.)

From the minutes of the meeting of the directors held on August 22, 1939 (Dulin being absent):

"COMPENSATION
OF SECRETARY
AND TREASURER

The meeting then proceeded with a discussion of the amount of compensation being paid by the company to J. C. Ballagh as its Secretary and Treasurer, and the recommendation was made that his salary as such officer be increased to the extent of $4,000.00 per year as of March 1, 1939, on a basis whereby said increase would be paid in four equal quarterly installments commencing on June 1, 1939, and continuing until further order of the Board.

Thereupon, on motion of Director Armington, seconded by Director Miller and carried, Director Ballagh not voting thereon, it was

RESOLVED, that commencing as of March 1, 1939, the compensation being paid by this cor-

poration to J. C. Ballagh as its Secretary and Treasurer shall be and the same is hereby increased to the extent of $4,000.00 per year on a basis whereby such increase shall be paid in equal quarterly installments of $1,000.00 each, commencing on June 1, 1939, and continuing until further action of this Board." (R., 229.)

From the minutes of the meeting of the directors held on March 18, 1940:

"COMPENSATION
OF PRESIDENT

The meeting then proceeded with a discussion of the subject of increasing the compensation of the President to the extent of $500.00 a month, commencing as of the 1st day of March, 1940, at the suggestion of Director Ballagh. It was pointed out that under the administration of the President a number of economies had been effected and that the affairs of the corporation were being so operated as to materially enhance the net profit being derived from its activities, and further that the amount of earnings currently being experienced were more than sufficient to justify said increase. Director Dulin stated that he had no objection to making an increase in the compensation being paid to the President but expressed himself as feeling that the same should not be made for any definite period and with the understanding that it should not remain in effect beyond any reversal in the current trend of favorable business conditions.

"Thereupon, on motion, duly seconded and carried, Director Miller not voting thereon, it was

RESOLVED, that the compensation being paid by this corporation to De Mont G. Miller, its President, for his services as such, shall be and the same is hereby increased as of March 1, 1940, from the sum of $1,000.00 per month to the sum of $1,500.00 per month, to continue until further action of this Board of Directors and with the understanding that the same may be decreased in the event of the appearance of a reversal in the current trend of favorable business conditions.

"COMPENSATION
OF SECRETARY-
TREASURER

The President then suggested that the Directors consider the amount of compensation being paid by the corporation to Director Ballagh, as the Secretary-Treasurer thereof, and pointed out that his services in addition to those of said office also include those of a sales manager, in view of the fact that Director Ballagh was and had been for many years in complete charge of all sales activities of the corporation. The statement was made that during the last few months there had been sharp increase in the volume of sales and that the efforts devoted to the business of the corporation by Director Ballach had been showing very satisfactory results. The suggestion was made that the monthly compensation being paid Director Ballagh be increased to the

extent of $1,000.00 a month and that the quarterly compensation being paid to him remain the same. Director Dulin stated that he objected most strenuously to the suggested increase and expressed himself as feeling that the same was entirely unwarranted and should not be put into effect under any conditions until the corporation was paying satisfactory dividends to its shareholders.

"Thereupon, on motion of Director Miller, seconded by Director Burrell and carried, Director Dulin voting in the negative and Director Ballagh not voting thereon, it was

RESOLVED, that the monthly compensation being paid by this corporation to J. C. Ballagh, its Secretary and Treasurer, for his services as such and in the supervision of the sales activities of this corporation, shall be and the same is hereby increased as of March 1, 1940, from the sum of $1,000.00 per month to the sum of $2,000.00 per month, to continue until further action of this Board of Directors and with the understanding that the same may be decreased in the event of the appearance of a reversal in the current trend of favorable business conditions;

FURTHER RESOLVED, that the quarterly compensation being paid by this corporation to J. C. Ballagh, its Secretary and Treasurer, for his services as such and in the supervision of the sales activities of this corporation in the amount of $1,000.00 a quarter shall remain the same and shall not be deemed to have been

changed or modified by the foregoing resolutions." (R., 242.)

From the minutes of the meeting of the directors held on November 29, 1940 (Dulin not present):

"ADDITIONAL
COMPENSATION
TO J. C.
BALLAGH

The President then suggested that the Directors consider the payment of additional compensation for the current fiscal year to Director Ballagh, and pointed out that he had been serving as the Secretary and Treasurer as well as the Sales Manager of the company and that due to his efforts the company had been enjoying an exceptionally fine volume of business and that its earnings were being materially increased, with excellent prospects for a further increase during the next fiscal year. Director Armington suggested that Director Ballagh be paid additional compensation for his services during the current fiscal year in an amount equivalent to one-sixth of his regular compensation paid or payable to him by the company for said year.

"Thereupon, on motion of Director Armington, seconded by Director Burrell and carried, Director Ballagh not voting thereon, it was

RESOLVED, that the proper officers of this corporation shall be and they are hereby authorized and directed to pay to J. C. Ballagh as additional compensation for his services

rendered to the company during the fiscal year ending on November 30, 1940, a sum equivalent to one-sixth of his regular compensation paid or payable to him by his corporation for his services during the current fiscal year.

"Additional Compensation to D. G. Miller

The subject of paying additional compensation to Director Miller, the President of the corporation, was then brought up for discussion and the extent and value of his services rendered during the current fiscal year were reviewed in detail. After a consideration of said services the suggestion was made that he should be additionally compensated by the company therefor to the same extent as other executives in that his services were of a comparable value.

"Thereupon, on motion of Director Ballagh, seconded by Director Armington and carried, Director Miller not voting thereon, it was

Resolved, that the proper officers of this corporation shall be and they are hereby authorized and directed to pay to D. G. Miller as additional compensation for his services rendered to the company during the fiscal year ending on November 30, 1940, a sum equivalent to one-sixth of his regular compensation paid or payable to him by this corporation for his services during the current fiscal year." (R., 251.)

From the minutes of the stockholders' meeting held on January 21, 1941:

"RATIFICATION
OF PRIOR ACTS
OF OFFICERS
AND DIRECTORS

Thereupon, on motion of J. C. Ballagh, seconded by D. G. Miller and carried, E. S. Dulin voting in the negative, it was

RESOLVED, that all action taken by the Board of Directors of this corporation since the date of the last annual meeting of the shareholders, whether said Directors were de facto or de jure, and all action of the officers of this corporation done pursuant to the authorization of the Board of Directors or with the knowledge and acquiescence of the Directors are hereby ratified, approved and confirmed as and for the corporate acts of this corporation.

"E. S. Dulin explained his vote in the negative on the foregoing resolution by stating that in his opinion the acts of the officers and Directors in accepting and fixing the amount of compensation paid during the last fiscal year to the President and Secretary was contrary to the best interests of the minority shareholders." (R., 264.)

No. 10,473

IN THE

United States Circuit Court of Appeals

FOR THE NINTH CIRCUIT

BYRON JACKSON CO., a corporation,

Appellant,

vs.

PATTERSON-BALLAGH CORPORATION, a corporation, J. C. BALLAGH and D. G. MILLER,

Appellees.

APPELLEES' BRIEF.

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APPELLEES' BRIEF.

Supplementary Statement of Facts.

Respondents concur generally in the accuracy of appellants' "Concise Statement of the Case" down to the second paragraph on page 4 of its brief. There it is stated that, shortly after defendant Miller acquired the shares of Patterson, the Board of Directors "was revamped in a manner dictated by Ballagh and Miller and thereafter consisted of Ballagh, Miller, one Howard Burrell * * *, one H. C. Armington * * * and E. S. Dulin, plaintiff's president." There is a footnote (App. Br. p. 5), "Dulin could not be dislodged; there was cumulative voting."

The real facts are that on August 4, 1938, long before Mr. Miller became a stockholder or connected with the Company, the Board of Directors of the corporation was increased from three to five members [R. 165-167], and, following this amendment of the by-laws, Messrs. J. C. Rennie and H. W. Elloitt were elected as the two additional members of the Board, the three then members being defendant J. C. Ballagh, C. L. Patterson and E. S. Dulin, plaintiff's president, *all of whom were present and voting.* The elections of Messrs. Rennie and Elliott were unanimous, *Dulin voting therefor* [R. 168]. The election of directors for the year 1939 occurred at the annual stockholders' meeting on January 27, 1939, at which time the five previous directors, to wit, Messrs. Patterson, Ballagh, Elliott, Rennie and Dulin were re-elected, *Mr. Dulin and plaintiff corporation both participating in the vote* [R. 198].

Defendant Miller did not acquire Patterson's stock nor succeed him as a director and officer until some time in February, 1939 [R. 211]. Director Rennie resigned at a special meeting of the Board on February 10, 1939 [R. 209] and defendant Miller was *unanimously* elected in his place. *Director Dulin seconded defendant Miller's nomination and voted for his election* [R. 211]. At this same meeting Patterson resigned as president and as a director and defendant Miller was nominated and *unanimously* elected president, *Director Dulin seconding his nomination and voting for his election* [R. 212]. At the same meeting H. C. Armington was nominated and elected a director in the place of Patterson, resigned, *Director Dulin seconding Armington's nomination and voting for his election* [R. 213]. At a special meeting of the Board on June 27, 1939, Director Elliott resigned [R. 220] whereupon Howard Burrell was elected in his place, *Director Dulin, the president and "representative*

of plaintiff," as he asserts, both seconding Burrell's nomination and voting for his election [R. 221].

This is the record notwithstanding the attempt in the language quoted from pages 4 and 5 of appellant's brief, to represent that the selection of directors Armington and Burrell was "dictated by Ballagh and Miller." Every step in the change of the personnel of the Board, which took place over a considerable period of time, was prominently participated in by plaintiff's president and representative Dulin and, of course, approved by him.

The footnote on page 5 of appellant's brief is equally misleading. There was never at any time any thought, suggestion or intimation of a desire on the part of defendants, or anybody else, to "dislodge" Dulin as a director and we suggest that this footnote is injected gratuitously as a further effort to misrepresent the situation. The facts are, and the record so shows, that the directors, including the defendants, were at all times solicitous of Dulin's prerogatives as a director and deferential to him in a high degree. For example, at a meeting of the Board of Directors on December 20, 1938, when matters of some importance were under consideration, the following entry appears in the minutes:

> "Mr. Ballagh then stated that when this matter was discussed at a previous meeting, Mr. Dulin had expressed the wish to have the matter of Mr. Rennie's employment held over until a later meeting to allow him time to study it over. Mr. Ballagh further stated that, inasmuch as Mr. Dulin was not present to vote, he preferred to not vote on the question." [R. 196.]

Upon a divided vote held during a directors' meeting on January 27, 1939, both Messrs. Patterson and Rennie voted with Mr. Dulin [R. 202]. The minutes of a

special directors' meeting on November 29, 1940, contains the following entry [R. 247-248]:

> "The Secretary (defendant Ballagh) reported that he had been advised by Director Dulin that he would be unable to attend the meeting and that he hoped the same would be adjourned until the following week so that he could be in attendance. It was pointed out to the Directors that there were certain matters which should be completed before the end of the current fiscal year of the company on November 30, 1940, and it was agreed that only such matters would receive attention and that all other matters for consideration would be placed before the Board at an adjourned meeting when Director Dulin could be in attendance."

The record is wholly devoid of any evidence whatever that anything was ever done violative of Mr. Dulin's complete rights as a director and stockholder.

At the top of page 5 of appellant's brief it is said that defendants were employed only as "President and General Manager" (Miller) and "Secretary and Treasurer and Sales Manager" (Ballagh) according to the minutes which appear in evidence as Plaintiff's Exhibit 1. As to the year 1939 and defendant Ballagh, the reference should be to R. 201 where defendant Ballagh was elected "Secretary-Treasurer" for that year. As to defendant Miller and 1939, the reference should be to R. 212 where defendant Miller was elected "President." Miller was never elected "President and General Manager" nor was Ballagh ever elected "Secretary and Treasurer and Sales Manager" as asserted by appellant for the years 1939, 1940 and 1941 which are in question here, but were for

each such year elected merely as "President" and "Secretary and Treasurer," respectively [R. 200, 238, 267]. In the same paragraph at the top of page 5 it is said "the defendants were employed only in the capacities above stated. *They were not employed as research men or inventors.*" (Emphasis appellant's.) And on page 6 of its brief appellant says:

> "Although the defendants in the trial court did not expressly concede that they were forced to resort to their claimed services as inventors in order to justify the amounts of their salaries, they did in several ways impliedly make such a concession."

This is a gratuitous and false assertion not justified by anything whatever in the record and it is furthermore wholly immaterial; that the defendants were conducting experiments and working as inventors was at all times known by all stockholders, directors and interested parties as the record shows and at numerous directors' meetings the progress of experimental work is referred to and discussed [R. 170, 186, 189, 194, 202], the legal effect of all of which will be hereinafter discussed.

Appellant asserts in the second paragraph on page 5 of its brief that the Board was "dominated" by Ballagh and Miller who "dictated" the policy of the corporation and reference is made to certain oral testimony. Mr. Ballagh testified that the company policies were outlined by the president and himself "subject to the action of the board" [R. 354]. Mr. Miller testified that the policies were outlined by himself "within my realm as president and with the approval of the board" and that Mr. Ballagh directed the policies in his own department [R. 381] just

exactly, we submit, as is done in any other corporation. It is next stated on page 5 that the new board, over the objections of Dulin representing plaintiff, "did three things of importance." First, it is said, it renounced the royalty agreement [Exhibits 15-a, 15-b, 15-c, and 15-d] with plaintiff corporation. This it did by advice of counsel as a pure legal and business proposition, on the theory that its monopoly under the Bettis patent having failed when that patent was declared invalid, it should no longer dissipate funds of the corporation by paying royalties for something it was not receiving. Surely this is consistent with defendants' duty to the corporation as its directors and Dulin's position in this regard was consistent only with his interest in plaintiff Byron Jackson & Co. which desired to continue receiving royalties at the expense of defendant corporation whether plaintiff was entitled to them or not. It is stated that, secondly, defendants discontinued paying dividends. This is true and there were many reasons why it should have discontinued to pay them at the time, as the record reveals [R. 361, 382, 383, 384]. Thirdly it is asserted that marked increases, being those complained of by plaintiff, were made in the salaries of Ballagh and Miller. This is true and the responsibilities and duties as well as the value of the service of both Mr. Ballagh and Mr. Miller were tremendously increased.

Just as soon as the Bettis patent was declared invalid the sales of the commodity which had constituted the corporation's principal stock in trade tremendously slumped [R. 478, 479, 480].

It was realized by the directors of the corporation that substituted articles must be developed and the duty of doing this devolved upon defendants Ballagh and Miller. They responded to this duty [R. 401, 431, 432, 433, 434, 435, 440, 449].

And as the result of the inventions which they did develop commencing with the end of the year of 1938 the volume of business and profits of the corporation were not only maintained but increased which otherwise would not have been the case [R. 126, 151, 199, 235].

At the conclusion of its purported statement of facts, (App. Br. p. 7), appellant asserts that the two questions involved in this appeal are:

> "(a) Were the salaries of Ballagh and Miller excessive? and
>
> (b) Did the plaintiff waive its right to so claim?"

If these were the only questions in the case there would be nothing for the Court to do but to dismiss the appeal. The gravamen of plaintiff's case is fraud and conspiracy and the payment of allegedly excessive salaries *as the result thereof*. Unless the fraudulent conspiracy is proven, plaintiff's whole case must fall to the ground and the statement just quoted would seem to be a waiver of the allegation of fraud and tortious wrong in the complaint.

ARGUMENT.

The Scope of the Reviewing Power of the Circuit Court of Appeals on This Appeal.

At page 42 of appellant's brief the following statement appears:

> "We point out that not only is this an equity case, but also that under rule 52(a) of the Rules of Civil Procedure, where findings are made by the court without a jury, the appellate court is not limited to the mere question whether there is any substantial evidence to support the findings, but may set them aside if against the clear weight of evidence (State Farm Mut. Automobile Ins. Co. v. Bonacci, 111 Fed. (2d) 412)."

We challenge the statement that this is an equity case in the first place, and, in the second place, the correctness of the statement relative to the power of the Appellate Court in reviewing questions of fact and findings of fact made by the trial Court where a law action is tried to the Court as the trier of fact, rather than to a jury.

Considering the latter of these two propositions first, we believe the true rule as to the power of the Appellate Court to review facts and findings of fact made by the trial Court, is correctly stated in the following cases:

Sundt v. Turman Oil Co. (C. C. A. Tex., 1940), 107 F. (2d) 762;

Great Atlantic & Pacific Tea Co. v. Grosjean (1937), 301 U. S. 412, 420, 57 S. Ct. 772, 81 L. Ed. 1193, 112 A. L. R. 293, rehearing denied 302 U. S. 772, 58 S. Ct. 3, 82 L. Ed. 599;

Borden's Farm Products Co. v. Ten Eyck (1936), 297 U. S. 251, 261, 56 S. Ct. 453, 80 L. Ed. 669;

Murphy v. Sun Oil Co. (C. C. A. Tex., 1937), 86 F. (2d) 895. Cert. den. 300 U. S. 683, 57 S. Ct. 754, 81 L. Ed. 886, wherein the Court said:

"The evidence other than documentary was all given orally. The District Judge heard the witnesses, and we are bound by his findings unless they are unreasonable, *that is, wholly without support in the evidence.* We cannot find them so." (Italics ours.)

Western Union Telegraph Co. v. Nester (C. C. A. Cal., 9th Cir., 1939), 106 F. (2d) 587. Certiorari granted ..... U. S. ....., 60 S. Ct. 468, 84 L. Ed. .....

This case was subsequently reversed by the Supreme Court of the United States, 309 U. S. 582, 84 L. Ed. 960 on other grounds.

Cherry-Burrell Co. v. Thatcher (C. C. A. Mont., 9th Cir., 1940), 107 F. (2d) 65. [See Appendix p. 1.]

Storley v. Armour & Co. (C. C. A. 8th, 1940), 107 F. (2d) 499. [See Appendix p. 1.]

Crowell v. Baker Oil Tools, Inc. (C. C. A. 9th), 99 F. (2d) 574. [See Appendix p. 2.]

Incidentally in the case of

State Farm Mut. Automobile Ins. Co. v. Bonacci, 111 Fed. (2d) 412,

the only case cited by appellant in support of its assertion, the facts are that the record in the trial court consisted largely of documentary evidence as distinguished from oral testimony, which fact the Circuit Court of Appeals for the Eighth Circuit specifically mentions in justification of its reversal of the findings of fact of the District Court. [See Appendix p. 3.]

Consequently the case cited is not authority for the power of the appellate Court to review facts found by the trial Court in a case where the testimony is principally oral as in the case at bar.

This Is an Action at Law and Not a Suit in Equity.

The question as to whether this is a suit in equity or an action at law is important not only with reference to the power of the appellate Court to review findings of facts but also in determining upon which party the burden of proof rests and the extent and character of that burden of proof. Respondents contend that the case is an action at law in the nature of a tort action, the alleged wrong being grounded in fraud and conspiracy to commit fraud. The remedy sought is a money judgment in favor of the corporation in a categorically definite amount. No accounting, injunctional relief or other equitable remedy of any kind is asked nor is any necessary in order to afford plaintiff the relief which it seeks, assuming only that it proves its allegations of fact by a fair preponderance of the evidence as in other tort actions.

To determine whether the action is legal or equitable, resort must first be had to an examination of the complaint itself.

The only allegations in the complaint entitling plaintiff to any relief (other than formal allegations relative to the parties, jurisdiction, stock ownership in defendant corporation, prior demands, etc.) are contained in paragraphs IV, V, VI, VII, VIII, and IX.

In paragraph IV it is alleged that the Board of Directors consisted of five persons of whom three were Dulin, president of plaintiff, defendants Ballagh and Miller "and other persons who were selected by such directors by, and in fact were and are representives of, the said Ballagh and the said Miller upon the said board"; and

that defendants Ballagh and Miller "by means of their said stock ownership and by means of their said representation upon the Board of Directors of said corporation by themselves and by their said representatives * * * at all times * * * have dominated, controlled and directed, and do now dominate, control and direct each and every of the acts and doings of the said defendant corporation." Paragraph V alleges that the defendants Ballagh and Miller "have fraudulently and unlawfully connived, cooperated, schemed and conspired and do now fraudulently and unlawfully connive, cooperate, scheme and conspire in directing the affairs of the said corporation for their own ends as distinguished from the well-being of said corporation and the interests of plaintiff as a minority stockholder thereof and for their own profit * * *."

Paragraph VI merely alleges that, as a part of the scheme and conspiracy alleged in paragraph V, defendants Ballagh and Miller as directors of defendant corporation together with the other directors (excepting Dulin), who are their "representatives," declared and paid to defendant Ballagh excessive salary and compensation in *certain specific amounts* for the year 1939, 1940 and 1941. The paragraph does not seek an accounting but alleges *in exact figures* what plaintiff deems to be reasonable compensation for defendant Ballagh for each year, the amount actually paid as such and *the exact amount of the claimed excess.*

Paragraph VII is identical in language with paragraph VI excepting that it relates to the compensation paid to defendant Miller.

Paragraph VIII alleges that plaintiff has received no dividends from defendant corporation at any time since February 15, 1939, and that, on information and belief, defendants Ballagh and Miller arranged to be paid alleg-

edly excessive salaries for the three years in question for the purpose of depriving plaintiff of dividends.

Paragraph IX alleges that "said defendants Ballagh and Miller are indebted to said defendant corporation in at least the sum of $41,416.66, no part of which has been repaid by the said Ballagh or by said Miller or by either thereof to the said corporation." This is obviously nothing but a common count at law in *indebitatus assumpsit* for a specific amount which is the exact difference between the amounts alleged to have been actually paid to defendants Ballagh and Miller in the years 1939, 1940 and 1941 and the amounts alleged to have been reasonable compensation for each of them for these years as set forth in paragraphs VI and VII.

The prayer for relief asked for judgment "against said defendants Ballagh and Miller in the sum of $41,416.66 with interest, etc." It will be noted that separate judgments are not asked against the defendants Ballagh and Miller notwithstanding the fact that the excess payments claimed as to each of them in paragraphs VI and VII differ widely, the excess as to Ballagh claimed in paragraph VI being $30,166.66 whereas the excess claimed as to Miller in paragraph VII is $10,250. A joint judgment against both is sought in the full amount exactly as a judgment for the full amount of plaintiff's damage would be sought against joint tort feasors in an action at law. This fact is important in determining whether the action is legal or equitable, and also in considering the equitable status of a plaintiff which presumes to seek in a court of equity a judgment in the sum of $41,416.66 against a defendant who, even according to its own allegations, can owe no more than $10,250 and against another who, according to its allegations, can owe no more than $30,166.66.

Much loose language appears in the opinions of Courts in cases where derivative actions are brought by minority

stockholders to recover allegedly excessive compensation paid to officers and directors, either on behalf of themselves "and all other stockholders similarily situated" or on behalf of the corporation itself as in this case, to the effect that such actions are equitable in their character. Having read literally hundreds of such cases, we confidently state to the Court that in no case have we found an action of this character treated as a suit in equity where some equitable relief has not been sought in the complaint or applied by the Court. The usual equitable relief sought or applied in such cases is an accounting. This is sometimes accompanied by injunctional relief of some character and in many cases a receiver is sought. In the case at bar, however, as appears clearly from the face of the complaint, no equitable relief of any kind is asked nor is any necessary to afford plaintiff the complete remedy it seeks. The complaint cannot possibly be regarded as stating a cause of action other than at common law to recover damages against joint tort feasors, the tort consisting of a fraudulent conspiracy.

The Court's official record shows that on Friday, July 3, 1942, "this cause came on for further trial without a jury" [R. 35] and on July 6, 1942, "this cause coming on for further non-jury trial, etc.", both of which entries are strongly corroborative of the idea entertained by all parties at the time that the case was one at law being tried to the court as the trier of facts rather than to a jury.

Under these circumstances the Courts, wherever the question has been raised, have uniformly held such derivative actions brought against corporate directors to be actions at law and not suits in equity. This question occasionally becomes highly important and fundamental. For example, if the action is one at law the defendant should not be deprived of his constitutional right to a jury trial. In some states a different statute of limitations applies

to actions at law and to suits in equity and, in some, as in California, in a suit in equity an appeal lies to the Supreme Court of the State, whereas in an action at law, the appellate Court of last resort is the intermediate appellate court. Thus the Courts have been called upon to pass upon the question as to whether actions of this character are at law or in equity and, tested by the standards laid down in those decisions an examination of the complaint in this case establishes conclusively that this is an action at law tried to the Court rather than to a jury with the apparent acquiescence of both sides.

In the early case of

O'Brien v. Fitzgerald (N. Y.), 38 N. E. 371,

the receivers of a banking corporation, themselves the creatures of equity, sued directors to recover back amounts which it was alleged the corporation had lost by reason of their wrongful conduct. Obviously the plaintiff receivers were suing in a derivative or representative capacity for the benefit of the corporation. The Court says:

> "There is no suggestion that any equitable relief is essential to a full and complete redress, and no facts are stated which indicate a need of such intervention. It is not averred that a discovery is requisite to the completeness of the remedy. On the contrary, the acts of negligence are asserted as fully known, and capable of proof. It is not alleged that an accounting is necessary to ascertain the damages, but these are claimed as a definite and fixed sum, resulting directly from the negligent acts of the defendants. It is not asserted that such defendants are severally liable for separate and personal misconduct, and in separate and different amounts, although that is a reasonable inference from the facts stated in the complaint, but it demands judgment against all and against each for the full amount claimed."

We submit that the foregoing language is exactly applicable to the case at bar. Much more might be quoted from the opinion to make the analogy even more complete. The Court of Appeals of New York held that the action was purely legal and in no sense equitable.

In

Cwerdinski v. Bent, 11 N. Y. Supp. (2d) 208,

which was a suit by a minority stockholder against the directors of the Bethlehem Steel Corporation to recover for the corporation certain very large bonuses paid to officers and where a six-year statute of limitations applied to actions at law whereas a ten-year statute of limitations was applicable to suits in equity, the result was the same. [See Appendix p. 3.]

The authorities which govern the question in the case at bar are collated and discussed ably by Judge O'Brien in

Potter v. Walker, 276 N. Y. 15, 11 N. E. (2d) 335.

The Court held that the action was legal and not equitable and that the six-year and not the ten-year statute of limitations applied. Plaintiff, as a minority stockholder in the Pan American Petroleum and Transport Co., brought a derivative action against directors of the corporation for acts allegedly committed by them, including the allegedly wrongful payment to one of them of the sum of $150,000. In the complaint an accountting is asked but the Court holds that, as to this particular cause of action, none is needed since the amount of the alleged loss to the corporation was directly asserted in the complaint, that consequently an action at law affords a complete remedy, no resort to equity is required, the action is therefore legal and not equitable and the six-year and not the ten-year statute of limitations applies. In the

course of the opinion the New York Court of Appeals quotes from

Wallace v. Lincoln Savings Bank (Tenn.), 15 S. W. 448, 24 Am. St. Rep. 625,

an opinion written by Mr. Justice Lurton, later a distinguished member of the Supreme Court of the United States. [See Appendix p. 4.]

The same question arose in the case of

Becker v. Empire Power Co., 31 N. Y. Supp. (2d) 914.

This was a suit by minority stockholders against officers and directors of a corporation *"for an accounting in equity"* to recover alleged unlawful profits obtained by them at the expense of the corporation. The Court held the action to be one at law and not in equity. [See Appendix p. 5.]

The decision of the Court of Appeals of the State of New York in

Dunlop v. Dunlop, 34 N. E. (2d) 344,

was followed in the case just cited. The opinion is *per curiam.* [See Appendix p. 5.] The obvious effect of this opinion is that where no equitable remedy is required as in the case at bar, the action is one at law and not one in equity even though it be one brought by a minority stockholder in a derivative capacity to recover profits gained by corporate directors who "have profited in any degree through a breach of their fiduciary duties" which is the claim here.

An early New York case of the same character,

Dykman v. Keeney, 48 N. E. 894,

involved the question of the right of defendants to a trial by a jury. The Court in a well reasoned opinion dis-

cusses the situation at length, cites and quotes many authorities and holds that an action at law affords a complete remedy, that the defendants should not be deprived of their constitutional right of a trial by a jury and that the action is strictly legal and in no sense equitable.

The same question arose in a different connection in the case of

Gormley v. Slicer (Ga. Sup. Ct.), 172 S. E. 23.

It was an action by the State Superintendent of Banks on behalf of depositors, stockholders and creditors of a defunct trust company against the latter's trustees who, the opinion says, occupy the same status as the directors of a corporation, to recover losses occasioned by their negligence in administering the affairs of the bank. If the action was equitable in its nature an appeal would lie direct to the Supreme Court of the State, whereas if it were legal in character, such an appeal would not lie. The question was certified to the Supreme Court which held the action to be purely legal in character although the reference to that Court shows that the case involves complicated and numerous items covering a period of years which it would be difficult to present to a jury. [See Appendix p. 6.]

In

Potter v. Walker, 287 N. Y. Supp. 812,

which was later affirmed by the Court of Appeals in the case of the same title reported in 11 N. E. (2d) 335, *supra*, the whole question is most thoughtfully and carefully analyzed and discussed and with the same result. [See Appendix p. 6.]

In

Emerson v. Gaither et al. (Md.), 64 Atl. 26,

the Court quotes from Clark and Marshall on Corporations and Judge Thompson's article on corporations in 10 Cyc. [See Appendix p. 8.]

The same principle is recognized by the Federal courts.

Corsicana Nat. Bank v. Johnson (C. C. A. 5th), 218 Fed. 822,

was an action against an officer of a national bank to recover alleged losses resulting from the defendant's violation of a Federal banking statute. The Court reached the same result on this question. [See Appendix p. 9.]

See also the majority opinion by Mr. Justice Holmes in

Curtis v. Connly, 257 U. S. 260, 66 L. Ed. 222.

In those states where courts have held that a stockholder's derivative suit to impose liability on directors is one in equity (although in every such case we have been able to find, an equitable remedy is either sought or applied as we have already stated), the rule seems to prevail that a corporation director is a trustee of the corporation, its stockholders and creditors to the same extent and with the same duties and liabilities as is a trustee of an express trust.

The better rule is that, while a trustee occupies a fiduciary relationship to the corporation, its stockholders and creditors, that relationship is one of agency and in the director's dealings with the corporation and its property his fiduciary liability is the same as that of an agent to his principal and not that of a trustee of an express trust to his *cestui que* trust. That is the rule in California.

In

Ballantine's Manual of Corporation Law and Practice, 1930 Edition, Sec. 122,

it is said:

> "As was stated in a former section, it is sometimes said that the directors and other officers of a corporation are trustees for the corporation, but, strictly speaking, this is not true. The relation is that of principal and agent, and is governed by substantially the same rules as govern a similar relation between material persons."

In the recent case of

Bainbridge v. Stoner, 16 Cal. (2d) 423,

an opinion by the Supreme Court of California decided in 1940, which was a suit brought by directors and minority stockholders of a corporation to have another director declared trustee of certain mining claims for the benefit of the corporation and its stockholders, the Court says with reference to the status of a corporate director:

> "However, strictly speaking, the relationship is not one of trust, but of agency, although it has been held that a director must comply with the requirements of Section 2230 of the Civil Code relating to trustees."

This appears to be the last pronouncement of the Supreme Court of California on the subject.

It must be admitted that, in the case at bar, California law is controlling. Defendant is a California corporation. The two individual defendants are citizens and residents of that state and all of the transactions complained of occurred therein. It consequently seems conclusive that the status of the defendant directors is that of agents for the corporation, that the action against them is purely one at law to recover a definitely alleged sum of money in a joint judgment against them by way of damages allegedly

sustained by the defendant corporation as the result of their tortious conduct amounting to a fraud committed upon it and, as the result of which, it is claimed the defendant corporation's stockholders, including plaintiff, have indirectly suffered. All of this being true, it necessarily follows:

First, that the reviewing power of the Appellate Court as to issues of fact and the findings made thereon by the trial court, are narrowed and restricted as compared with what would be the case if the suit were one in equity; and

Second, that the burden rests upon plaintiff to prove the alleged tortious wrong claimed to have been committed by the individual defendants and the resulting damage by a fair preponderance of the evidence just as in any other tort action at common law.

Irrespective of Whether the Case at Bar Be One at Law or in Equity, the Burden of Proof Is Upon the Plaintiff.

The first section of the argument in appellant's brief, pages 22-25, inclusive, consists of an attempt to establish that:

> "due to the relationship of the (individual) defendants to the corporation it was not only unnecessary for plaintiff to establish fraud, but a presumption arose in plaintiff's favor that the salaries were excessive."

The foregoing seems to us a most extraordinary statement and means that in any case a minority stockholder in a corporation might commence an action by drawing a complaint alleging fraud and the payment of excessive salaries to officers and, as the result thereof and by filing and serving this complaint, he would, *ipso facto*, have made out a *prima facie* case.

Later the following statement appears:

> "When directors of a corporation are in this position (by which we suppose is meant that they are also majority stockholders) a minority stockholder, in order to force restitution by the directors to the corporation, need not establish fraud; there, also, arises a presumption that the salaries were unreasonable and the burden of proof is upon the directors to show the contrary."

According to appellant, no proof whatever by plaintiff is required either to establish fraud or any other wrongdoing nor that the salaries complained of are excessive. The mere allegations in the complaint are all that is required and, as will be seen, are all that plaintiff has produced in the case at bar to support its contention.

Obviously this is not the law and to contend that it is, certainly should throw discredit upon appellant's entire case.

As stated, this case and the conduct of the parties herein are governed by the law of the State of California.*

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*Section 311, C. C. P., provides in part:

"No contract or other transaction between a corporation and one or more of its directors * * * shall be either void or voidable by reason of the fact that such director or directors are present at the meeting of the Board of Directors or a committee thereof which authorizes or approves such contract or transaction or that his or their votes are counted for such purpose, if:

"(a) the fact of such * * * financial interest be disclosed or known to the Board of Directors or committee and noted in the minutes and the board or committee authorize, approve or ratify such contract or transaction in good faith by a vote sufficient for such purpose without counting the vote or votes of such director or directors; or

"(b) the fact of such * * * financial interest be disclosed or known to the shareholders and they approve or ratify such contract or transaction in good faith by a majority vote or written consent of shareholders entitled to vote; or

"(c) the contract or transaction be just and reasonable as to the corporation at the time it was authorized or approved.

"Such common or interested directors *may be counted in determining the presence of a quorum at such meeting.*" (Italics ours.)

All of the essentials of this statute were complied with in connection with each corporate action complained of by plaintiff. The sole claim which plaintiff can make under this statute is under subsection (c) on the issue as to whether the transactions complained of were "just and reasonable as to the corporation" at the time they were authorized and approved. Plaintiff says they were not and the defendants say they were. Obviously, it is the duty of plaintiff to sustain its contention by a preponderance of the evidence as in other cases.

As the Court knows, there are in the State of California certain statutory presumptions, many of which are directly applicable to the situation here.*

Each and every one of these presumptions cloaks the two individual defendants in this case and, taken as a whole, are sufficient to surround the transactions complained of and every element thereof. Number 1, until it has been overthrown by evidence, absolves them from the tortious fraud, conspiracy and wrong alleged by plaintiff. Number 7 establishes, *prima facie,* and until overthrown by evidence produced by plaintiff, that the compensation paid to them was due them. Number 11, *prima facie*, establishes that the compensation received by them belongs to them until the plaintiff has proven otherwise. Number 15 cloaks the official acts of directors of defendant corporation with regularity until plaintiff has proven irregularity and fraud by evidence. Number 19 estab-

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*Section 1963, C. C. P., defines forty rebuttable presumptions, among which are:

"1. That a person is innocent of crime or wrong;
"7. That money paid by one to another was due to the latter;
"11. That things which a person possesses are owned by him;
"15. That official duty has been regularly performed;
"19. That private transactions have been fair and regular;
"20. That the ordinary course of business has been followed;
"33. That the law has been obeyed;
"39. That there was a good and sufficient consideration for a written contract."

lishes, *prima facie*, the fairness and regularity of all the corporate acts complained of by plaintiff until it has satisfied the burden of proof devolving upon it by evidence, and the same thing is true of Number 20. Number 33 establishes *prima facie* that the defendants in doing whatever they have done acted lawfully.

A resolution of a corporate board of directors for employment and fixing compensation is a contract in writing and has mutuality.

27 C. J., Sec. 307, pp. 257-258;

Western Timber Co. v. Kalama River Lumber Co. (Wash.), 85 Pac. 338, 114 Am. S. R. 137, 6 L. R. A. (N. S.) 397, 7 Ann. Cas. 667.

Therefore, there is here a statutory presumption that both defendants Ballagh and Miller rendered "a good and sufficient consideration" for the compensation paid them by defendant corporation.

Solely as the result of the statutes of the State of California, it is clear that the burden is upon the plaintiff to prove both elements of its alleged case, that is; first, the fraudulent conduct of the individual defendants, and; second, the alleged overpayments for their services: both by a preponderance of the evidence.

Indeed this is the universal rule.

In

Presidio Mining Co. v. Overton (C. C. A. 9th Cir.), 261 Fed. 933,

a case decided by this Court in 1919, in which the opinion was written by Mr. Justice Morrow and which was a suit brought by minority stockholders for a variety of types of equitable relief, including an accounting, injunctive relief and a receivership and therefore necessarily cog-

nizable in equity, the Court says on the question of burden of proof (page 940):

> "The minority stockholder is entitled to the protection of a court of equity against the illegal and fraudulent acts of the majority; but the misconduct of the majority must be clearly established to justify the court in such interference. *Here, as elsewhere, fraud is not presumed, but must be proved.* Lewisohn v. Anaconda Copper Min. Co., 26 Misc. Rep. 613. 56 N. Y. Supp. 807-818." (Italics ours.)

And again at page 960 of the opinion it is said:

> "The burden of proof was upon the plaintiffs to prove the illegal and fraudulent character of the salaries paid to the directors and officers in San Francisco."

It will be borne in mind that the foregoing was admittedly an equity case and not purely an action at law, as is the case at bar.

In

> *Gamble v. Queens County Water Co.* (N. Y.), 25 N. E. 201,

a minority stockholder's suit seeking to enjoin the issuance of corporate stock and bonds and in an opinion by Mr. Justice Peckham, later of the United States Supreme Court, which case is cited with approval by the California District Court of Appeal, Third Appellate District. In *Fornaseri v. Cosmosart Realty Corp.,* 96 Cal. App. 549, later to be commented on, the New York Court of Appeals places the burden of proof upon the plaintiff and says that "a case must be made out which plainly shows" that the actions complained of are wrongful and not for the best interests of the corporation.

Spiegel v. Beacon Participations, Inc. (Mass.), 8 N. E. (2d) 895,

was a minority stockholder's suit in equity to recover from the directors alleged loss to the corporation resulting from the purchase for the corporation of a large note which it was claimed was worthless. On the issue of burden of proof the court says:

> "Commonly, the burden of proof in a suit by or in behalf of a corporation against its officers or directors is on the plaintiff to show misconduct." (Citing many cases, p. 905.)

And again:

> "As already pointed out in our opinion the burden of proof is on the plaintiff to show the loss sustained by the defendant by the misconduct of the several defendants."

Schmitt v. Eagle Roller Mill Co. (Minn),

which is a minority stockholder's case of the same character, is to the same effect and it is there said:

> "There is no presumption that the directors acted in bad faith or unjustly." (P. 282.)

Nahikian v. Mattingly (Mich.), 251 N. W. 421,

was an action brought by three minority stockholders to force a director and officer to repay alleged excessive salaries, unauthorized expense moneys, royalties received on a patent, to assign a patent to the company, to turn over certain shares of stock held by him in trust for the company, to pay indebtedness owed by him to the company and to remove him as president, director and general manager. The court holds that the burden of proof is upon the plaintiff. The court's remarks, not only on

the issue of burden of proof but on the entire question of excessive salary payments, are so pertinent as to justify quoting. [See Appendix p. 10.]

In

Bates Street Shirt Co. v. Waite (Me.), 156 Atl. 293,

which was a suit in equity to recover from former directors money alleged to have been fraudulently converted to their use by way of alleged excessive salaries and otherwise, or illegally expended by them, the court says:

> "The burden of proving that the salaries are excessive is on the complainant. Presidio Mining Co. v. Overton (C. C. A.), 261 Fed. 1023 and if fraud is alleged the proof must be clear and convincing." (Citing cases, p. 298.)

And, at the conclusion of the opinion:

> "Plaintiff has not sustained the burden of proving these charges. On the contrary, there is much to prove that defendants conducted the business of the corporation with fidelity and integrity."

The same rule is announced in

Chapman v. Troy Laundry Co. (Utah), 47 Pac. (2d) 1054,

which was a derivative suit brought by minority stockholders against corporate directors seeking to cancel certain shares of stock allegedly improperly and fraudulently issued. [See Appendix p. 12.]

In

Savory v. Berkey (Minn.), 2 N. W. (2d) 146,

another minority stockholder suit seeking to recover from corporate directors for the benefit of the corporation,

losses allegedly sustained by the latter as the result of misappropriation of corporate funds, the court says:

> "With the charges of misappropriation and wrongdoing made by plaintiff he, of course, had the burden of proof."

Bodell v. General Gas & Elec. Corp. (Del.), 132 Atl. 442,

a suit of a similar character, the court held similarly. [See Appendix p. 12.]

In

Cole v. National Cash Credit Ass'n. (Del.), 156 Atl. 183,

which is a suit of the same general type, clearly in equity and seeking injunctional relief, the result is the same. [See Appendix p. 12.]

Karasik v. Pacific Eastern Corp. (Del.), 180 Atl. 604,

was a suit in equity for injunctional relief by corporate stockholders against officers and directors of the corporation, claiming the squandering and wasting of large amounts of corporate money. The court holds the burden of proof to be on plaintiffs. [See Appendix p. 13.]

And in

Anderson v. Bean (Mass.), 172 N. E. 647, 72 A. L. R. 959,

which was a suit by certain beneficiaries of a trust against the trustee, in which, it should be pointed out, the defendant was actually the trustee of an express trust and not merely an agent as are corporate directors, the result is the same. [See Appendix p. 13.]

See also:

Beha v. Martin (Ky.), 171 S. W. 393.

In

Venus Oil Corp. v. Gardner (Ky.), 50 S. W. (2d) 537,

which was a case identical in principle with that at bar, there was a judgment in favor of plaintiff in the trial court for the return of salaries in the sum of $27,625 which the Appellate Court reversed on appeal, saying in the second paragraph of the opinion "the burden is upon the objecting stockholders to establish affirmatively that the compensation allowed was unreasonable and excessive. Beha v. Martin, *supra.*"

Winberg v. Camp Taylor Dev. Co. (Ky.), 95 S. W. (2d) 261,

is substantially on all fours with the case at bar and the holding is the same. [See Appendix p. 14.]

In the complaint in this case there were allegations of fraud, irregularity, conspiracy, etc., and the court intimates that they are all mere conclusions without the allegation of any ultimate facts to support them and, as such, subject to demurrer. We submit that the same thing is true of the allegations of the same character in the complaint here.

In

Borg v. International Silver Co. (D. C. N. Y.), 11 Fed. (2d) 143,

in which an injunction was sought by minority stockholders to prevent the sale of corporate stock, the court says:

"* * * and while the plaintiffs impute to the directors an ulterior purpose, and allege that they are

> not acting in the interest of the company, from all that appears there may be an honest difference of opinion as to what is best for the company. The position of director is one of trust for the benefit of the stockholders, and, until the contrary is clearly shown, it must be assumed that they are actuated solely by what, in their judgment, is best for the stockholders."

in denying plaintiff's motion for a temporary injunction. This decision was affirmed by the Circuit Court of Appeals for the Second Circuit in

> *Borg v. International Silver Co.,* 11 Fed. (2d) 147. [See Appendix p. 14.]

In

> *Noel v. Parrott* (C. C. A. 4th), 15 Fed. (2d) 669, Cert. den. 47 S. Ct. 457, 273 U. S. 754, 71 L. Ed. 875,

which was a suit by a taxpayer against the Collector of Internal Revenue, the plaintiff claiming that certain money received by him from a corporation was a gift and, as such, not taxable as income, the court says there is a presumption of regularity and honesty attending the official action of corporate directors. [See Appendix p. 15.] And this presumption was indulged by the court even though the directors were not parties to the action and certainly not in the position of defendants as to whom the well-nigh universal rule is that a plaintiff must prove his case by a preponderance of the evidence in order to prevail.

> *Gray Corp. v. Meehan* (C. C. A. 1st), 54 Fed. (2d) 223,

is to the same effect. [See Appendix p. 15.]

It therefore seems conclusive that the Federal courts follow the usual rule that where irregularities or fraud

are charged against corporate directors, the latter are protected by a presumption of regularity and honesty in their official acts which must be overthrown by evidence and that, in addition, the burden of proof is on the plaintiff; and this must necessarily be so where the transactions are governed by the laws of a state in which the same rule prevails, as is true in the case at bar.

The California decisions in both the Supreme Court and District Courts of Appeal follow the general rule already stated.

In

Snediker v. Ayres, 146 Cal. 407,

the California Supreme Court, after quoting portions of Section 2230 of the Civil Code, *supra,* says:

> "The plaintiff alleged fraud and collusion on the part of the directors, and the burden was on him to establish these allegations. The findings show the contrary."

Certainly no language could be more apt than the foregoing to dispose of plaintiff's contention relative to the burden of proof in the case at bar.

In

Fornaseri v. Cosmosart Realty etc. Corp., 96 Cal. App. 549,

plaintiffs were stockholders and creditors of the defendant corporation in which the corporate directors were joined as defendants and it was sought to recover from them certain funds allegedly held in trust for the corporation which had been realized from the sale of a certain lease and option belonging to the corporation. The court holds that the presumptions favor the defendants and the burden of proof is on the plaintiffs. [See Appendix p. 16.]

In

Michaels v. Pacific Soft Water Laundry, et al., 104 Cal. App. 366,

which was a suit by stockholders questioning the validity of a corporate election and in which a rehearing by the District Court of Appeal and a hearing by the Supreme Court of the State were both denied, the court reaches the same result. [See Appendix p. 16.]

And again in

Clark v. Oceano Beach Resort Co., 106 Cal. App. 574,

plaintiff stockholder sought to enjoin the sale of his stock in the corporation contemplated because of his failure to pay an assessment theron. It was claimed that the assessment was levied as the result of a conspiracy between certain of the directors with the intent to oust other stockholders and obtain the control of the corporation and the trial court so found. The Appellate Court reverses the trial court, and announces the same rule. [See Appendix p. 17.] In this case also a petition for rehearing before the same court and a hearing by the Supreme Court of the State were denied. It would seem conclusive that the rule in California is as contended by respondent and that this Court in passing upon a purely California transaction involving the internal affairs of a California corporation is bound by this rule.

Appellant's Cases Distinguished.

To support its extraordinary contention that no proof is necessary either to establish fraud or that the salaries complained of were excessive and, in effect, that all that is necessary to cast on defendants the burden of disproving these claims is to commence an action in which the complaint alleges them, appellant first cites the case of

Stratis v. Anderson (Mass.), 150 N. E. 832,

from which case it quotes an excerpt which we submit from a reading of the entire case is wholly misleading and deceptive. This was a minority stockholder suit seeking to recover alleged excessive salaries for the benefit of the corporation. The opinion starts out by saying:

> "The case was referred to a master. Since there is no report of the evidence, his findings of fact must be accepted as final and true."

Immediately preceding the excerpt quoted by appellant from this case the court says:

> "It is not necessary to inquire nicely into the relative rights of the parties where the majority of the directors who are disinterested fix a salary by vote for an associate in participating in the vote."

That is exactly what occurred in the case of each vote of the directors in fixing the salaries of the individual defendants in the case at bar. Upon none of the ballots did the defendant officer participate in the vote fixing his own salary as the minutes show and as will be subsequently pointed out. In the *Stratis case* there were three directors, each of whom was an officer and the salary of each of whom is complained of. Each officer participated in the vote as to his own salary. The books are full of cases condemning directors for participating in the votes determining their own salaries. That, however, is not the case here. Neither Mr. Ballagh nor Mr.

Miller participated in any vote relative to his respective salary, which fact totally distinguishes the case at bar from the *Stratis case* as the Massachusetts court says in the language above quoted. In the excerpt quoted by appellant from the *Stratis case* are cited many cases which it is claimed support the position asserted by appellant. We can say confidently that none of them does as applied to the facts in the case at bar.

In the case of

Von Arnim v. American Tube Works (Mass.), 74 N. E. 680,

a minority stockholder suit against corporate officers and directors for alleged misappropriation of funds, the court says at the commencement of its opinion:

> "Under a bill of complaint brought by a minority stockholder against the officers of the corporation for official misconduct by which its assets have been wrongly appropriated, *it is obligatory for him to allege and prove that they have failed to perform their duty, thus causing a breach of their trust;*" (Italics ours)

which obviously is directly contrary to the assertion and claim of appellant in this regard and is excellent authority for the contention of respondents.

In

Meyer v. Ft. Hill Engraving Co. (Mass.), 143 N. E. 915,

next cited which was also a minority stockholder's suit seeking to recover alleged excessive salary and in which the directors were joined as defendants, there was a judgment for defendants. affirmed on appeal because of plaintiff's failure of proof and on the issue of the burden of proof the court says:

> "The burden of proving mismanagement, and alleged wrongful appropriation of the moneys of the com-

> pany *was on the plaintiff*. The judge saw and heard the witnesses upon whose evidence, in some respects conflicting, the question depended, and his finding, 'I am not satisfied the payments to Ioos, Freyer and Yeaton have been excessive,' cannot be said to be plainly wrong. Revere Water Co. v. Winthrop, 192 Mass. 455, 459, 78 N. E. 497." (Italics ours.)

This case is also excellent authority for respondents here and we suggest could hardly have been read by appellant before citing it to this Court.

> *Godley v. Crandall & Godley Co.* (N. Y.), 105 N. E. 818,

also cited by the Massachusetts court, was a minority stockholder suit for an accounting and to compel the return of moneys distributed to officers and directors in proportion to their stock holdings and without relation to any services rendered by them. There is no word at any place in the opinion concerning the burden of proof but a fair reading and interpretation of the opinion certainly leads to the conclusion that the Court assumed the burden to be on plaintiff even though the suit was one necessarily in equity.

> *Green v. National Advertising, etc. Co.* (Minn.), 162 N. W. 1056,

sought an accounting, the appointment of a receiver and other equitable relief and was brought by plaintiff who owned one-half of the corporate stock, against defendants who owned the other one-half. At no point in the opinion is the question of the burden of proof even referred to. We have already cited and quoted from Minnesota cases which clearly establish the rule in that state as being in accordance with the contention of respondents here.

Lillard v. Oil Paint & Drug Co. (N. J.), 56 Atl. 254

is likewise entirely silent on the question of burden of proof and the subject is nowhere even referred to in the opinion of the court and the same thing is true in the report of the same case contained in 58 Atl. 188 which is confined solely to the question of costs.

Booth v. Beattie (N. J.), 118 Atl. 257

is likewise devoid of any reference whatever to the burden of proof upon the respective parties but certain language contained therein seems particularly appropriate on the merits of the case subsequently to be considered. [See Appendix p. 17.]

The memorandum opinion in the same case reported in 123 Atl. at page 925 is likewise silent on the subject.

The last case cited in the quotation from the *Stratis case, supra,* is

Sotter v. Coatesville Boiler Works, et al. (Pa.), 101 Atl. 744.

At no point in the opinion is there even the merest reference to the question of burden of proof but the Court evidently proceeded on the theory that the burden is on the plaintiff as in other cases even though the suit is one in equity seeking an injunction. [See Appendix p. 18.]

The foregoing should effectively dispose of the case of

Stratis v. Anderson, supra,

and the cases cited by appellant in the excerpt which it quotes from that decision, all of which are, in reality, authority for respondents' position on the point being considered.

Appellant next cites

Geddes v. Anaconda Copper Mining Co., 254 U. S. 590, 65 L. Ed. 425

and quotes an excerpt from that opinion. This suit was brought by minority stockholders of the Alice Gold & Silver Mining Company, all of the stock of which had been sold to defendant Anaconda, claiming that the stock of the Alice Co. had not been properly evaluated in the transaction. Among the grounds of attack was the fact that the sale was negotiated by two boards of directors (of the two companies involved) with a common membership and for an inadequate consideration. The facts were that the purchase of the Alice Co. stock was paid for by an exchange of Anaconda stock. The Court finds that the Anaconda stock had a definite money value on the New York and other stock exchanges and "* * * when stock which has an established market value is taken in exchange for corporation property, it should be treated as the equivalent of money, * * *." Where it clearly appeared as a matter of mathematical certainty that the consideration for the purchase assessed at its money value was inadequate, the plaintiff necessarily had sustained the burden of proof and the burden was thereupon cast upon the defendant to justify it. That is all that the quoted language from the opinion means. In addition, it might be pointed out that the directors of both corporations were the same and that they all participated in the official action of both boards with resulting personal profit to themselves, whereas in the case at bar neither of the individual defendants participated in the board action affecting himself.

In the excerpt quoted the Court cites

Twin Lick Oil Co. v. Marbury, 91 U. S. 587, 23 L. Ed. 328.

There is nothing in the opinion relative to the burden of proof.

Thomas v. Brownville etc. R. Co., 109 U. S. 522, 27 L. Ed. 1018

is also cited. Here also there is no reference to the subject of burden of proof but the Court does say relative to the allegations of fraud made by plaintiffs "these allegations are proved beyond question, and the Circuit Court held the contract void and the bonds issued in fulfillment of it also void, and dismissed the bill." This must surely mean that plaintiffs not only sustained the burden of proof but proved their case conclusively by evidence.

The next case cited in this excerpt is

Corsicana National Bank v. Johnson, 251 U. S. 68, 64 L. Ed. 141.

This was an action brought by a national bank against a former director to hold the latter liable in damages for allegedly making illegal loans. Not only is this case no authority for appellant's contention relative to the burden of proof but it is direct authority contrary thereto as the language of the opinion in several places clearly indicates. In this regard it is perhaps sufficient to quote the second section of the syllabus which reads:

> "What weight should be given to substantial evidence tending to support the plaintiff's view of disputed facts is for the jury, not the court, to determine."

Appellant next cites and quotes from the case of

Davids v. Davids, 120 N. Y. Supp. 350.

The corporation involved here had a capitalization of $30,000. There were three directors and their three salaries were attacked by a minority stockholder. The total of these three salaries was originally and had for years been $6,750. The three directors, all participating in the action, raised this total for their own benefit to $24,000. For the year prior to this action on their part, the corpo-

ration had earned approximately $6,000 and during the year succeeding sustained a loss of about $1,000. In the excerpt from the opinion quoted by appellant it appears "that they had voted themselves salaries by a resolution in which they all joined." At another point in the opinion the Court says:

> "They met *and voted themselves* this large increase in salary by a single resolution in which they all concurred." (Italics ours.)

The distinction between the *Davids case* and the case at bar, of course, is that in the *Davids case* the beneficiaries of the resolution themselves voted for it. As has previously been pointed out, the courts very generally condemn conduct of this kind where the recipient of the compensation, being a director himself, participates in the action of the board. This factor is not present in the case at bar which entirely distinguishes the two cases and renders the *Davids case* wholly inapplicable to the present situation.

Next is cited

Schall v. Althaus, 203 N. Y. Supp. 36.

In this case the compensation attacked consisted of bonuses given at the end of the year for which the compensation, by way of salaries, had already been fixed. It also appears that each of the officers who was also a director participated in the vote for his own salary and bonus and the Court further says:

> "It does not appear, however, that there was any substantial increase in the duties and responsibilities of the defendants."

In the *Schall case* therefore the distinguishing factors of the *Davids case* are also present and in addition, as will subsequently appear, in the case at bar the compensation awarded to the individual defendants did take into ac-

count extremely important and valuable increases in the duties and responsibilities of the individual defendants and the considerations moving from them to the corporation.

Appellant next cites the case of

Carr v. Kimball, 139 N. Y. Supp. 253.

In that case the corporation again had three directors, one of whom was a relative of the defendant Kimball who the Court found controlled and dominated the corporation and owned a majority of the stock therein, excepting for five shares which he gave to his relative and five additional shares which he gave to the third director. All of the three directors participated in the vote increasing their own salaries.

Certain other equities favoring the plaintiff in the case were that he had formerly been a principal officer, that he had invented and developed certain lines which constituted approximately fifty per cent of the corporation's business, that he had been ousted from his official position and employment by the corporation by the defendant Kimball and the other two directors whom Kimball dominated, pursuant to a prior threat that this would be done unless he consented to an increase in Kimball's salary and that there were no increases in the duties or responsibilities of the officer directors who received the increased compensation complained of.

Appellant next cites

Ross v. Quinnesec Iron Mining Co., 227 Fed. 337.

This case involved a very complicated state of facts and was a suit by a minority stockholder seeking relief against the payment by defendant corporation to the firm of Corrigan, McKinney & Co., of commissions upon the sales of products produced by subsidiaries of the defendant corporation. The Court finds from the evidence that Corri-

gan, McKinney & Co. controlled the board of directors of defendant corporation as well as their own "and thus in effect were on both sides of the contract." This fact plaintiff, no doubt, proved by a preponderance of the evidence. The Court merely holds that when a situation such as this appears the burden is cast upon the defendant directors of both corporations to establish that the contract was a fair and reasonable one. In other words the defendant directors themselves participated, presumptively for their own benefit. in their official action as directors of both the corporations, which is not the situation in the case at bar as has been pointed out.

Church v. Harnit, 35 Fed. (2d) 499

next cited by appellant is a case of the same general character and involved the validity of bonuses given to employee-officers of a corporation who were also directors. The method of allowing and paying these bonuses was peculiar. At a meeting of the board consisting of five members, a bonus was voted to the President Harnit by the other four directors, he himself not voting. Thereafter, and when this amount had been placed to his credit on the books of the corporation he himself would divide it up as he saw fit and out of it pay bonuses to certain of the others. In other words, the directors who voted the bonus to Harnit in the first place were, in fact, voting a bonus to themselves since it was understood in advance that Harnit would pay portions of the bonus voted to him to them and, under these circumstances, the Court holds that the burden was upon the directors voting for the bonuses which they eventually received to show that they were fair and reasonable. [See Appendix p. 18.]

In the lower court the plaintiff's bill was dismissed and this was affirmed on appeal, it being found that the com-

pensation was fair and reasonable This is simply another of many cases which hold that where a director does himself participate in the vote affording him increased compensation without a corresponding increase in his duties and responsibilities. the burden is cast upon him to establish his fair dealing, which is not at all the case at bar.

The next case cited is

Jordan v. Jordan (Conn.), 109 Atl. 181.

In this case no question of salary was involved. The corporation required additional funds as capital because of increased business and sought to obtain them from one Sisk who was elected a director of the corporation. The suit involves an investigation of the financial transactions between Sisk and the company. Sisk would discount accounts and receivables of the corporation for cash. The claim was, in effect, that the discount he received for doing this and the profits he personally made in selling certain property of the corporation were excessive and unconscionable. A mere reading of the facts would seem to demonstrate that this was true. While the trial court found that the burden was on the company's receiver to prove fraud, the Appellate Court very properly holds otherwise.

The situation on the face of things showed the realization of large profits by Sisk on each of the transactions complained of which alone gives rise to a presumption that the property which he obtained from the corporation and resold was worth appreciably more than the price at which he obtained it from the corporation. This is obviously a very different situation from the one with which we are concerned.

next cited, was a suit for an accounting by stockholders against the president of a corporation who had taken from the corporation a commission of twenty-five per cent for selling corporate stock. Such a commission or any commission to the defendant president had never even been authorized by a meeting of the board of directors. The Court considers whether the president may be entitled to keep what he has been paid on a *quantum meruit,* entirely aside from any authorization by the board. [See Appendix p. 18.]

The Appellate Court granted a new trial.

The last case cited by appellant on this point is

Davis v. Thomas A. Davis Co. (N. J.), 52 Atl. 717.

The suit is one by stockholders to compel three directors and officers of defendant corporation to return "all or a portion of the salaries which these three directors *voted to themselves.*" (Italics ours.) There were three directors and it clearly appears that they all participated in the vote of the board which resulted in the salaries complained of. Here again is a case, of which there are many, which lays down the rule that where the beneficiary of the vote participates in the voting, the courts will scrutinize the action of the board and the burden is shifted to the participating director to establish the fairness of the board's action. With this principle we have no quarrel but as repeatedly stated it is not applicable to the facts in the case at bar. We submit, and are confident that a careful analysis of the cases cited by appellant on the question of burden of proof will support the position of respondents where the facts are at all applicable, that such of the authorities as cast the burden upon the defendant are based upon facts not present in our case

which totally distinguish them. Many of the cases cited by appellant in support of its position are from the Appellate Division of the New York Supreme Court. The most recent case on the subject from that Court appears to be

Heller v. Boylan (1941), 29 N. Y. Supp. 651

which was an action by minority stockholders to recover "for the corporation from the company's directors for alleged improper payments to certain of the company's officers." Syllabus 6 of the headnotes reads:

> "In stockholders' derivative action to recover for corporation from corporation's directors for alleged improper payments to certain of its corporate officers on theory of waste, the burden of proof was on plaintiff stockholders."

Citing

> *Seitz v. Union Brass and Metal Mfg. Co.* (Minn.), 189 N. W. 586.

We have heretofore cited and quoted from numerous decisions of the New York Supreme Court and Court of Appeals which definitely establish the rule in that state, in cases where the facts are as they are here, to be in accordance with respondents' position.

We therefore submit that the power of this Court to review the facts, and the findings of fact made thereon in the court below, are subject to the limitation of the rule applicable to actions at law and that, whether the action be regarded as one in equity or at law, the burden of proof is upon the plaintiff to establish by a preponderance of the evidence both the fraud and the excessive compensation alleged.

An Analysis of the Proof Produced by the Respective Parties.

Assuming it to be established that the burden of proof is upon plaintiff to prove, first, a fraudulent conspiracy, and second, the payment of excessive salaries as the result thereof and, assuming further that on this appeal the findings of fact of the lower court will not be disturbed if supported by evidence and unless clearly erroneous, an analysis of the testimony and the record on these two points is necessary.

In the first paragraph of its argument on page 22 of its brief, appellant makes numerous misstatements of fact as a mere reference to the record pages will demonstrate and the untruth of some of which has already been pointed out.

Appellant offered no testimony on the issue of fraud and conspiracy. Proof is wholly lacking on that issue.

The only evidence offered by plaintiff on the issue of excessive compensation which even tends to support its claims in that regard are the tabulation of its witness Bunch [Pl. Ex. 15, R. 438] printed at page 27 of its brief and the opinions and conclusions of plaintiff's president, Dulin [R. 387-417]. Bunch had been an "analyst and statistician," a stockbroker and "investment counsel," a "financial writer" and "public relation counsel" [R. 418]. His examination on *voir dire* [R. 419 *et seq.*] should certainly demonstrate his lack of competency as a witness on this issue. An objection to his testimony was overruled [R. 422]. Plaintiff's Exhibit 15 which he had prepared was admitted without objection [R. 436] though it is obviously the rankest kind of hearsay and incompetent on innumerable grounds. There is nothing whatever to show any reasonable comparison between the business of defendant corporation and any of the concerns listed in the exhibit nor between the particular exigencies confronting these concerns, if any, and the very decided crisis and necessity for developing new products and an increased volume facing the defendant. Neither is there anything to show, nor was there any opportunity to cross-examine, concerning the number of executive employees

working for the concerns listed on the exhibit in addition to those receiving the "two highest salaries" or the nature and extent of the work of such other employees supplementing that of the recipients of the two highest salaries. The merest consideration of this exhibit at once demonstrates its inadmissibility as evidence, but even more, its total lack of any probative value in establishing the contentions of plaintiff. Most of the cases which have passed upon the subject have held both, that what may be paid employes in some other business than the one under consideration, and also, what the individual has earned or might earn in some other employment, are immaterial in cases of this kind. The sole question is, *what are the services of the individual whose compensation is questioned actually worth to the corporation by which he is employed.*

> *Fletcher Cyc. Corporations,* Perm. Ed. Vol. 5, Sec. 2180, p. 501 and cases there cited.

We submit, without wasting any more space on it, that Exhibit 15 contains no evidence worthy of consideration.

As to Dulin's testimony on the issue of whether the salaries complained of are reasonable or not, he admits that he favored an increase in the salaries of Messrs. Patterson and Ballagh made by the board in October, 1938, from $1,000 to $1,500 per month each [R. 388-389], and also the increase in Mr. Miller's salary from $1,000 to $1,500 per month voted at a meeting in March, 1940 [R. 389]. Mr. Dulin's testimony may be searched in vain for anything whatever going to the issue of whether the compensation paid to defendants *is reasonable.* In fact there is nothing on the question in any part of his testimony excepting reference to his having voted against certain increases and having objected thereto, all of which, naturally, proves nothing.

Appellant's only other witnesses were called in rebuttal solely for the purpose of giving their opinions of the value of the various inventions developed by the defendant officers, the rights in which the latter assigned to the corporation [R. 510, 514, 520, 527, 530.]

The first of these was the witness Grant [R. 542-550]. He was a purchasing agent employed by a well-drilling contractor, with very limited experience and practically none in any oil producing area other than California [R. 549]. He had had no experience with the lip protector or any of the other inventions devised by defendant officers [R. 548] and without consuming further space we submit that his testimony has neither probative value in support of appellant's case nor anything to rebut the case of respondents for which sole purpose it was produced.

Appellant's only other witness is one Chestnut [R. 565-579], an employee of appellant who was also called to rebut respondents' testimony relative to the value of the inventions devised by respondents for the corporation. Here again a reading of the entire testimony demonstrates conclusively that it proved nothing whatever affirmatively to support appellant's allegations of fraud, wrongdoing and excessive salaries and has little or no value in rebutting respondents' case as to the value to defendant corporation's business of the inventions designed by Messrs. Ballagh and Miller for which sole purpose it was produced.

We therefore have a case where plaintiff alleges fraud. conspiracy and tortious conduct as the result of which the individual defendants procured excessive salaries to be paid to themselves. As for testimony to establish these charges plaintiff offers absolutely nothing whatever on the issue of conspiracy, fraud and tortious conduct and nothing on the question of reasonable compensation other than the incompetent Bunch exhibit [App. Ex. 15], and Dulin's testimony relative to certain objections which he made to some but not all of the increases complained of.

No wonder appellant argues that the law only requires the filing of a complaint to prove its case. It literally has nothing else. On this state of the record alone the presumptions favoring defendants compel a decision in their favor.

Respondents, however, prove their case by evidence. Their oral testimony was that of Messrs. Ballagh, Miller, and Burrell, all directors, and Mr. Morris, an employee.

Mr. Ballagh, the real originator of the business, gives a history of his own background, the commencement of the business which later resulted in the incorporation of the company, and of the latter's business from the time of its incorporation [R. 472-542]. The business first consisted of the manufacture and sale of so-called pipe line protectors made of rubber, the purpose of which he describes [R. 475]. This device was patented by one Bettis with whom a licensing agreement was made in 1927 [R. 476]. In 1929 the sales of this item were $1,111,000. In 1930 they were $636,000. In 1932 they dropped to $149,000 and in that year the Bettis patent was declared invalid by the U. S. District Court [R. 478], as the result of which some sixty competitors commenced marketing the same or a similar product [R. 479]. This situation necessitated the development of other or "non-protector" items for sale, the first of which was marketed in 1936 (retread rubber and not invented articles) [R. 479]. Mr. Ballagh devoted practically all of his time during daylight hours from the latter part of 1938, to the work of the corporation and spent at least three nights a week at home working on various inventions and other sales work for the company. He acted as sales manager and had charge of the advertising [R. 483] and in addition handled certain important patent litigation both in Oklahoma and California [R. 484]. He took no vacations [R. 483]. As the result of this Ballagh devised a number of new articles for manufacture and sale, among which were the lip protector, the nature and purpose of which he describes [R. 510-514], the Hydraulic applicator [Defendants' Exhibit J, R. 489-505], the sucker rod protector [R. 487, 521, 528], the pipeline wiper [R. 489, 514, 518, Defendants' Exhibit M], the Kelly wiper [R. 519, 521] and a plastic tubing protector [R. 523, 530]. The nature, purpose of and gross profits on all of these items are described much better by Mr. Ballagh in his oral testimony than we can attempt to describe them here. We should point out, however, that the lip protector is an improvement on the invalidated Bettis protector, the nature of which Mr. Ballagh describes, and on which the company has no competition [R. 510-514] and that the Hydraulic applicator affords an im-

proved means for installing protectors on the pipe which further reduces competition on protectors generally and has resulted in acquiring for the company many new customers in the mid-continent field and in California, among which are the Associated Oil Company, The Shell Company, the Union Oil Company, the Barnsdall Company, the Richfield Oil Company, Bellridge Oil Company and the Texas Company [R. 505]. All of these devices were developed and placed on the market from about the beginning of 1939 [R. 401] and during the three-year period here involved. Each of them has more than doubled in sales in each successive year as is graphically shown by the chart [Defts. Ex. G, reproduced in the Appendix, p. 53]. The actual sales figures year by year are given in Mr. Ballagh's testimony [R. 487-488], which, however, do not reflect the value of the Hydraulic applicator and lip protector inventions, the effect of which is to eliminate competition on and increase protector sales formerly protected by the invalidated Bettis patent.

Miller became president on February 15, 1939, and, in addition to performing his duties as such, managed the factory, attended to the finances, purchasing and did certain inventing. Up to the time of the trial he had invented the steel-clad open hole stabilizer, the steel-clad protector, the rod protector [R. 373], a rod wiper and two line wipers [R. 374]. The progressive sales by years on these items are shown in the chart [Defts. Ex. A, and the figures in dollars and cents are given in Miller's oral testimony [R. 376-377].

The testimony of Mr. Morris, [R. 459-472] who was a salesman in the defendants' employ in the mid-continent field, describes the use of the various devices developed by defendants Ballagh and Miller, their practical elimination of competition in the territory with which he was familiar and their effect upon the sales volume of the company.

Mr. Burrell [R. 428-446] gives as his reasons for approving Mr. Ballagh's compensation, the great amount of time and effort devoted by him to the company's sales, the important part he played in patent litigation in Oklahoma [R. 435], the perfection by him of the Hydraulic appli-

cator "which I consider the most important thing that had as yet been received by the company in the last few years" [R. 431], "a great many activities outside the ordinary course of his duties in developing articles and devices" [R. 433], the development of the lip protector [R. 435] and the development of the pipe wiper [R. 440]. As to his reasons for voting for Mr. Miller's compensation, he testifies that Miller, being in charge of the finances, the operations of the factory and the purchasing of supplies had caused an improvement in the financial condition of the company, that the ratio of assets to liabilities was improved, that he had installed various efficiencies in the plant and office [R. 433], that he was engaged in the development of certain new products and that Mr. Dulin had no objection to the increase [R. 434]. As to the compensation to both Messrs. Ballagh and Miller in so far as the matter of inventions was a factor, it was Mr. Burrell's opinion that the inventions belonged to the inventors in the absence of assignments or licensing agreements. He testifies that they either had been or would be transferred as soon as invented or as soon as patents were applied for [R. 449] and that it was distinctly to the company's advantage to compensate Ballagh and Miller for the use of these inventions on a salary basis which was flexible from time to time depending upon the general condition of the business, rather than to definitely obligate the company to pay royalties under licensing agreements [R. 450-451]. Each of the inventions of Messrs. Ballagh and Miller and all rights therein including the patent rights already acquired and those applied for, were assigned by the inventor to the corporation and the corporation has manufactured and sold the items from the time of their invention royalty free. On this there is no dispute [R. 510, 514, 520, 527, 530].

Appellant claims, however, to have proven that respondents' compensation was excessive: that the compensation cannot be justified by respondents' claimed services as inventors, and that respondents' compensation was arranged as a part of a conspiracy between them to fraudulently enrich themselves at the expense of appellant and minority stockholders (appellant being the only one (App. Br. 48-52) under certain specific headings.

We will discuss each of these contentions in the order and under the headings in which they appear in appellant's brief:

"(a) *It* (the compensation) *was in excess of salaries paid by comparable but larger companies.*"

This whole argument is based on the Bunch exhibit [Pl. Ex. 15]. We believe what has heretofore been said should dispose of this exhibit as evidence. The argument is further vulnerable because of the evidentiary principle that what other employers pay to other employees is wholly immaterial, the only material question being what were the services of these defendants worth to the defendant corporation.

"(b) *The salaries paid to the defendants were several times greater than their prior compensation had been from other companies by which they had been employed.*" (App. Br. 28.)

In the first place what respondents have been paid in previous employments was wholly immaterial and inadmissible.

> *Fletcher's Cyc. Corp.,* Perm. Ed., Vol. 5, Sec. 2180, p. 501 and cases there cited.

The testimony was particularly objectionable as to the defendant Ballagh who, in reality, founded the defendant corporation's business in 1927 and has been employed by no one else than the defendant corporation and its predecessor partnership in the interval of approximately fifteen years. Obviously, the compensation which he may have received in any employment more than fifteen years previously was too remote to merit consideration, assuming it were admissible otherwise, nor was any comparison whatever sought in his examination relative to the duties in his previous employment as contrasted with those performed for defendant corporation.

Mr. Miller's employment elsewhere was more recent than Mr. Ballagh's. His examination on this point was objected to and erroneously overruled provisionally. The trial court never did finally pass on the admissibility of

the testimony (App. Br. 379). Here again nothing was elicited to permit a comparison between the value of the services rendered in some other employment and those rendered to defendant corporation.

We submit that appellant's argument under this heading is not worthy of any consideration by this Court.

"(c) *The salaries paid to the defendants were out of all proportion to the net profits of the corporation.*"

This, as are all the other arguments of respondent on the question of the reasonableness of defendants' compensation, is based largely on the incompetent and non-probative Bunch report [Pl. Ex. 15]. During 1939, 1940 and 1941, the years under consideration here, the management of the company was endeavoring to develop articles for manufacture and sale to take the place of the Bettis protector, the patent on which had theretofore been invalidated. This could only be done by developing new devices for use and sale in the general field of defendant company's activities, that is the field of oil well supplies, and this could best be done by inventing such new articles and devices. At this time it was not so much a question of current net profits but rather of investing time and money in developing additional products for the future. The determination of that policy was purely one within the discretionary powers of the Board of Directors of the company and the circumstances would, under all the decided cases, be very exceptional where a court would be justified in reversing or interfering with a policy of that kind determined by a corporate Board of Directors within the sphere of its proper jurisdiction. However, this policy as determined upon and carried out during the period resulting as it did in conferring upon the corporation a variety of new articles with which to supplement its line, did not decrease the company's earnings nor deplete its reserves. On the contrary its sales and earnings steadily increased during the period in question. [Pl. Ex. 4, R. 291.]

The consistent improvement in the earnings and financial condition of the company during the years 1939, 1940

and 1941 are reflected in the so-called Pennington audits [Pl. Exs. 5-A, p. 1, 5-B, p. 1 and 5-C, p. 2] as follows:

Net worth, end of year 1939	$243,598.42	
Net worth, end of year 1938	222,671.17	
Net gain for 1939		20,927.25
Net worth, end of year 1940	264,118.27	
Net worth, end of year 1939	243,598.42	
Net gain for year 1940		20,519.85
Net worth, end of year 1941	201,023.44	
Net worth, end of year 1940	181,802.80	
Net gain for year 1941		19,220,64

During these years the compensation to defendants complained of was being paid and, in addition to the net gains above shown for each year, an additional surplus for the period of $22,649.23 was accumulated to meet certain contingencies and particularly the contingent liability arising out of the suit brought by plaintiff for royalties on the invalidated Bettis patent which is now pending in this Court [R. 362]. These net gains for each of the three years remain after providing for all tax and other contingent liabilities including depreciation, as the audits will show. This means that at the end of the year 1939 the corporate stock had a book value of 243% plus, at the end of 1940, 264% plus and at the end of 1941 201% plus, based on a par value of $100 per share. The reason for the decrease in the book value between the end of 1940 and 1941 was the comparatively large amount set aside in the contingent reserve account in the interim and the elimination of $80,703.61 for goodwill as an asset. It will also be observed that during the three years the company earned, in 1939 $20.93 a share, in 1940 $20.52 per share and in 1941 $19.22 per share, all on a par value of $100 per share, which we submit is somewhat conclusive evidence of good management and the formulation of good business policy on the part of the company's

directors during this trying period. If these figures are compared with the profit and loss and capital and surplus figures shown on the Bunch exhibit [Pl. Ex. 15], the advantage is all with the defendant corporation. It is interesting to note that at the end of the three years in question there was available for distribution as dividends to the stockholders the following:

1939	$143,598.42
1940	164,118.27
1941	101,023.44

and, in addition thereto, there had been accumulated the reserve account above referred to by the end of 1941 and the item of goodwill theretofore carried as an asset in the sum of $80,703.61 was eliminated, notwithstanding which at the end of the year 1941 the stock still had a book value of $201 per share plus, as against the par value of $100 per share, and there remained $101,023.44 available for dividends. The fragmentary figures contained in appellant's brief at pages 29, 30 under this heading which are, for the most part, random monthly operating results for only *such* months as best suit appellant's purposes, are wholly misleading and do not give a fair representation of what the situation actually was.

Appellant concludes its argument under this heading by another reference to the Bunch figures [Pl. Ex. 15], which, it says, present no comparable cases except those where the particular company shown in the exhibit was either operating at a loss or "*had several times* more capital and surplus invested." The Court is probably sufficiently familiar with the general nature of most of the businesses listed in the exhibit to realize that most of them are engaged in heavy industry producing what are known as durable goods, a basic characteristic whereof is the investment of large amounts of capital producing comparatively small profits, and whose products sell on

very narrow margins of profit. The business of defendant corporation is not of this type at all. It produces highly specialized articles selling at a very high rate of gross profit. Its heart and life blood have little relation to the capital invested but are the development of efficient and non-competitive items in the field of oil well supplies. This could only be accomplished by invention and great activity in efficient marketing and, therefore, the success or failure of the business depends directly upon the accomplishments and activity of the individuals responsible for its operation rather than on its invested capital. These individuals were the individual defendants.

We believe this should effectually dispose of appellant's argument under this sub-heading.

"(d) *The salaries paid to the defendants were out of all proportion to the invested capital and the size of the business of the corporation* (App. Br. 31).

Appellant's argument under this heading has perhaps been sufficiently answered in respondents' reply under the last heading. Here again, the appellant's sole reliance is the wholly incompetent, irrelevant Bunch exhibit [Pl. Ex. 15], which, without a proper foundation to afford a comparison between the businesses listed thereon and that of defendant corporation or the services rendered for the "two highest salaries" and those rendered by defendant is quite without probative value. We desire to point out, however, that, even on the basis of the Bunch exhibit, defendant corporation's ratio of profit to capital and surplus even after paying the compensation complained of, accumulating a reserve against the contingent liability of the Byron Jackson Co. royalty suit and charging off the very large item of goodwill heretofore referred to, is approximately 11.5 per cent, which ranks eleventh in the list of the thirty-five businesses listed in the exhibit. We repeat, because it is an important factor in determining

the reasonableness of the compensations complained of in this case, that defendant corporation's business is one in which the size of the invested capital is a matter of comparative unimportance. The investment in an executive sufficiently expert, capable, resourceful and having the qualifications essential to developing and marketing essential products in the company's chosen field of operation is very much more important than is the investment of a large amount of money in heavy machinery which will produce tile and similar clay products, steel and metal articles or pulp and paper such as is being done by such concerns as Gladding McBean & Company, Western Pipe & Steel Company, Consolidated Steel Corporation and Puget Sound Pulp and Timber Company, to mention a few listed on the Bunch exhibit.

"(e) *The increases in defendants' salaries were made without any corresponding increase in the amount of the responsibility of the services rendered or to be rendered by defendants.*

We have already pointed out that prior to the invalidation of the Bettis patent and from the inception of the defendant company's business, the principal item which it sold was pipe line protectors licensed, and presumably protected, by the Bettis patent. In 1929 these sales amounted to $1,111,000. In 1930 this figure had dropped to $636,000 and in 1932 to $149,000. That was the year in which the Bettis patent was invalidated by the District Court [R. 478]. To make up for this drastic reduction in the sale of its article the company went into the business of making retread rubber, a staple, nonprotected, highly competitive article. It was realized, however, that other articles more closely related to the field of oil well supplies would have to be developed if the company were to survive [R. 479], and consequently Mr. Ballagh, as well as Mr. Miller as soon as he became connected with

the company, both of them experts in the field, turned their attention to the invention and development of such items but none of them was invented or developed prior to 1938 [R. 509].

Even Bunch had no information as to whether the executives receiving the "two highest salaries" in his exhibit "ever invented devices and gave them to the corporation royalty free" [R. 419]. He knew nothing whatever about the business of defendant corporation "except its financial data and the salaries that the officers draw and the general facts of its financial setup and operation." He didn't know anything about hydraulic applicators [R. 420] nor about the importance of protectors or pipe wipers [R. 421]. But he did know that patents and inventive rights in the oil business have a "very high value" [R. 423] and that businesses which have enjoyed very prosperous years have proceeded to lose money and lose their business to competitors due to some betterment of the article of their competitors [R. 424]. Incidentally, during the years when the business was depressed owing to the invalidation of the Bettis patent and between 1931 and 1939, there was paid a total of $30,418.42 to the plaintiff in dividends and royalties the greater part of which ($27,418.42) was for royalties on the invalidated patent [Pl. Ex. 18-D]. In support of its argument under this heading appellant cites certain cases each of which is readily distinguishable from the case at bar (App. Br. 33):

Schall v. Althaus, 203 N. Y. S. 36,

already commented on, involved bonuses given at the end of the year for which the salaries to be paid were already fixed and determined and were consequently mere gratuities. Also in each case the recipient director voted for his own salary and bonus and the court says:

> "It does not appear however that there was any substantial increase in the duties and responsibilities of the defendants."

which was most certainly not the situation in the case at bar.

Atwater v. Elkhorn Valley Land Co., 171 N. Y. S. 552,

next cited was about as different in its facts from the case at bar as could well be imagined. The corporation owned coal lands in West Virginia which it leased on royalty. There was nothing whatever to do but distribute the proceeds from the royalties. All the work was done by a $100 per month clerk. One Andrews was the president, Jones, his son-in-law, and Lee, the secretary, likewise a relative, were the directors. The latter two had been given their small amounts of stock by Andrews. On appeal, the secretary's salary was the only item involved. It appeared that he was a city employee working as such every day from nine in the morning until five in the afternoon; then he went to the company's office two nights a week; attended monthly directors' meetings and kept a rough draft of their minutes. There was no change of any kind in his duties or responsibilities.

Kreitner v. Burgweger, 160 N. Y. S. 256,

was obviously a very aggravated case from the standpoint of minority stockholders. The corporation had a capital of $250,000 and an accumulated surplus of $700,000 and had never paid more than four per cent in dividends notwithstanding the disproportionate surplus. There were three directors, directors representing the minority stockholders having been dropped from the board. All information relative to the affairs of the corporation was denied to the minority stockholders and could only be obtained by mandamus which had, on occasion, been done. $30,000 of the company's funds had been withdrawn by the officers and not accounted for. Political contributions and donations of various kinds had been made without authority

and there were no circumstances which could invoke the *quantum meruit* rule which will be later discussed. There were no increases whatever in the duties or responsibilities of the beneficiary directors and officers.

The last case cited by appellant under this sub-heading is

> *Raynolds v. Diamond Mills Paper Co.* (N. J.), 60 Atl. 941,

from which a short and misleading excerpt is quoted. The first purpose of the suit was to compel the declaration of a dividend and it was, consequently, one seeking relief in the nature of a mandatory injunction and therefore equitable in character. The second purpose was to compel the return by directors and officers "who had fixed their own salaries and drawn the amount of these salaries from the treasury of the corporation," whatever the court might find to be excessive. It is interesting to note the following comment of the court:

> "Now, we have these two, as it seems to me, radically different causes of action combined in one bill. No objection has been made to the joinder of these two causes of action."

Clearly implying that the first is equitable and the second legal in its character. The capital stock of the corporation was $300,000 and it had assets of a value between $500,000 and $600,000, had made large profits for the several preceding years and with these had steadily extended its business, acquiring more mills and machinery. However, the Court on the issue of dividends, decides the case in favor of the defendant. [See Appendix p. 19.] As to the salary issue this case differs from that at bar in the fundamental, which seems true of all the cases cited by appellant, that the compensation complained of was, in each case, determined by the affirmative vote of the beneficiary himself. [See Appendix pp. 19-20.]

The Defendants' Services Other Than Those Prescribed by the By-Laws.

Appellant prefaces its argument under its main title "3" commencing on page 34 of its brief, with a most unusual complaint. It dwells upon the "injustice" of permitting defendants to urge the value of their services rendered to the corporation for devising and inventing articles of manufacture and sale because, forsooth, "not one word was said about inventions or patents in plaintiff's complaint." After all, the defendants didn't draw the complaint. Appellant then bewails the fact that there was "no word of inventions or patents" contained in the answer and therefore "in all fairness" defendants' services in that connection "should not have been considered by the Court." It is difficult to imagine a more puerile wail than this. Plaintiff alleged that the defendants had been excessively paid. Defendants denied that allegation and naturally had a right to open up the entire field to show the exact nature and value of the services which they rendered the corporation for the compensation which it paid them.

"(a) *The by-laws of the corporation and the resolutions passed by its board of directors showed that the defendants were not being compensated as inventors.*"

Reference is first made to the by-laws of the corporation and the offices created thereby. The by-laws do not create any offices at all excepting those of *president, vice-president, secretary* and *treasurer.* [See Appendix p. 20.] The duties of the president as prescribed by the by-laws do not, no doubt owing to some oversight, appear in the record. The court, however, is familiar with the usual stereotyped provisions, customary in corporate by-laws, defining the duties of corporation presidents, which are usually confined to mere formal corporate acts, and it can, no doubt, properly take notice that the by-laws of the

defendant corporation do not differ from what is ordinarily the case in this regard. The duties of the secretary-treasurer were read into the record as a part of the testimony of defendant Ballagh [R. 485-486] and are of the stereotyped formal corporate character referred to. They include nothing relating to the management or promotion of sales, the development or invention of articles of manufacture and sale nor any other duties relating to the actual and productive purposes and aspects of the business.

At the annual directors' meeting of February 15, 1939, (206 *et seq.*), [Pl. Ex. No. 1] the following appears:

> "The meeting then proceeded with the matter of considering the compensation to be paid the president for his services and *the advisability of designating him as General Manager of the business and affairs of the corporation.*" (Italics ours.)

and a resolution was introduced and passed, *with the seconding by and the vote of Director Dulin,* appellant's president, that Mr. Miller be designated General Manager in addition to president. At a special meeting of the Board held on March 18, 1940 [R. 240, *et seq.,* Pl. Ex. 1], as to defendant Ballagh, it was "pointed out that his services in addition to those of said office (secretary-treasurer) *also include those of a sales manager,* in view of the fact that Director Ballagh was and had been for many years in complete charge of all sales activities of the corporation. The statement was made that during the last few months there "had been a sharp increase in the volume of sales and that the efforts devoted to the business of the corporation by Director Ballagh had been showing very satisfactory results." It therefore conclusively appears that the duties and responsibilities of defendant Miller were increased at the beginning of the

year 1939, which increase continued during all of the three years here in question, from those merely of president of the corporation as defined in the by-laws, to those of General Manager and that the duties of Mr. Ballagh were increased officially in March of 1940 from the formal duties prescribed for the secretary and treasurer in the by-laws to those of Sales Manager and further that it was officially recognized that he had been discharging the latter duties since at least the beginning of 1939 even though the official recognition of the increase in his duties did not occur until March of 1940. From a technical standpoint therefore, it clearly appears that the duties and responsibilities of both defendants were increased.

Technicalities aside and getting into the real merits and substance of the matter their actual duties and responsibilities as well as the value of the services rendered by each of them to the corporation, were tremendously increased by the invention and development of all of the various new articles of manufacture and sale which are enumerated and described in the record and which we will not take the space to re-enumerate.

To support its position under this heading the appellant first cites the case of

Stratis v. Andreson (Mass.), 150 N. E. 832.

We confess we do not see the point of the citation from appellant's standpoint. It appears to us that on this particular issue, as well as on others in connection with which we have previously analyzed the case, it is strong authority for the position of respondents. One of the defendants in that case whose compensation was complained of was employed as "treasurer, general manager and clerk" of the defendant corporation and he was paid separate salaries for each of these position "in the amounts of $6,000, $6,000 and $2,500 respectively, or $14,500 in

the aggregate." The facts in the case were referred to a special master who found that the compensation paid to this individual as a clerk was excessive and, therefore, the excess over the reasonable value of his services in that capacity should be returned by him to the corporation. The quotation from the case appearing at page 36 of appellant's brief is sufficient to dispose of appellant's point. If the individual defendants at bar had been paid *separate compensations* in their separate capacities as president, general manager and inventor in the case of Miller, or secretary-treasurer, sales manager and inventor in the case of Ballagh, it would, under the authority of the *Stratis* case be proper, if any competent proof were adduced by plaintiff to show that the compensation in any category was excessive, to inquire into that question. However, in the case at bar no separate compensation was paid to either Messrs. Miller or Ballagh for the different types and kinds of services they rendered to defendant. To use the language of the Massachusetts Court, their entire compensation was paid as a "unit" instead of being split up as it was in the *Stratis* case and, therefore, if "the entire compensation regarded as a unit was not excessive" and plaintiff has not sustained any burden of proof nor offered any competent proof at all that it was, its case must fall. Obviously on the point under consideration the *Stratis* case is no authority for appellant's position. Quite the contrary.

Appellant next cites

Lillard v. Oil Paint & Drug Co. (N. J.), 56 Atl. 254,

from which case a long quotation appears at page 37 of appellant's brief. The case involves a complicated statement of fact and corporate history and, because of the variety of relief sought, it was obviously equitable in

character. The sole issue of which the Court took any cognizance and for which it granted any relief finally boiled down to the reasonableness of a salary and the gist of it appears at page 260, quoted in the Appendix, p. 20. Incidentally, this is one of many cases holding that what one may have been paid in some other occupation or might earn in another employment is wholly immaterial to the question under consideration, the sole question being what are the services worth *in the particular employment under investigation.* In the *Lillard* case the Court specifically says that there have been no increases in either the duties or responsibilities for which the compensation was paid.

At page 38 of its brief, appellant seeks to twist an assertion in respondents' memorandum brief in the trial court into an admission that all respondents were entitled to be compensated for were the stereotyped formal services prescribed in the by-laws for the official corporate positions to which they had been elected. Whatever may have been said in the memorandum brief in the trial court is, of course, immaterial here, but what was there said contrasted cases where employees are endeavoring to recover compensation from a corporation, many of which were cited by appellant in the trial court, and cases such as this where a minority stockholder is seeking to recover back for the corporation compensation already paid by it to an employee. Obviously there is a great distinction. Respondents have never "conceded," nor do they now, that they "must look to the resolutions of the Board of Directors for such compensation as they received." They do contend, however, that they are entitled to compensation for their services as president, General Manager and for the development of inventions and devices so far as Miller is concerned, and as secretary-treasurer, Sales Manager and the development of devices and inventions so

far as Ballagh is concerned, paid in each case as a unit and not split up into separate categories as in the *Stratis* case, *supra,* and furthermore, as will later appear, that their services as General Manager and Sales Manager respectively, which are nowhere defined in the by-laws, resolutions or elsewhere were comprehended and understood by all of the stockholders and directors to include the development of devices and inventions for which they were to be compensated. As to these latter services, respondents claim they are entitled to compensation by reason of the well defined general understanding by the directors of the duties which were to be performed by them as General Manager and Sales Manager respectively, and in any event upon the *quantum meruit* theory.

"(b) *The services as inventors, for which the defendants claim compensation, were never performed for the corporation.*"

We are wholly at a loss to understand appellant's argument under this heading. Reference is first made to page 40 of respondents' trial memorandum from which a short quotation appears. Respondents' entire argument from which this quotation is excerpted, was to the effect that if the devices and inventions developed by the defendants had not been compensated for by the corporation by way of salary or otherwise as they were, and in the absence of their assignment by the inventor in each case to the corporation, they had been developed under circumstances which would constitute them the property of the inventor, all for the purpose of showing that for the compensation paid by the corporation to the inventors, the corporation gained great value which it otherwise would not have received and owned. Inasmuch as counsel has seen fit to quote a short excerpt from the argument presented in the trial court which

is obviously misleading, we quote the argument from which it was excerpted, in the appendix. [Appendix p. 20.]

Appellant next quotes excerpts from the testimony of Messrs. Ballagh, Dulin and Burrell, the obvious meaning of which is merely that, in the absence of compensation paid to Ballagh and Miller for their inventions and an assignment or an agreement to assign to the corporation, these inventions would have remained the property of the individual inventors. The fact, however, is, as has already been pointed out with appropriate reference to the record, that as the result of the common understanding between all the directors and parties interested, both Ballagh and Miller undertook their experimental work for the benefit of the corporation [R. 170, 186, 189, 194, 202] expecting to be paid therefor as they were by increased salary compensation [R. 382, 430-435, 440, 448-459, 564] and in every instance they assigned their patent rights, either actual or prospective, to the corporation [R. 449, 450, 527]. If under all these circumstances the inventions and devices were not developed for the corporation, it seems difficult to know for whom they were developed. After all, "the proof of the pudding is the eating thereof" and the corporation manufactured and sold all these devices and inventions from their inception royalty free, is still doing so and it owns by valid contracts of assignment in writing, all rights, patent and otherwise, present and prospective, in all of them. Appellant says that Dulin knew nothing about these inventions and cites page 406 of the Record. In the answer to the question as to whether Dulin knew about the inventive work Miller and Ballagh were doing, he says "I did not. During the period you are speaking of I was in Washington, at the request of the Government, over twenty times, and spent half of my

time outside the State of California." Under these circumstances it is obvious that Mr. Dulin was hardly in position to know much about the problems of the defendant corporation which he was supposed to be serving as a director. The minutes show, however, that experimentation and invention was discussed at numerous meetings [R. 170, 186, 189, 194, 204], and Director Burrell, a wholly disinterested party, testified that these inventions and devices were discussed "at practically every meeting" [R. 456, *et seq.*]. During the three-year period in question Dulin, even according to his own statement, spent altogether eighteen hours on the defendant corporation's business [R. 427] including "a substantial amount of time" which he says he devoted to the defendant corporation's affairs away from its premises and in his own office [R. 416]. It seems an obvious inference that Mr. Dulin was more interested in continuing to milk the defendant corporation for the benefit of Byron-Jackson & Co., of which he was the president, than he was in the welfare of the defendant corporation of which he was a director.

In concluding its argument under this sub-heading, appellant asserts that "authorities are to the effect that when an officer performs services outside of his duties he must have a contract with the corporation before he can recover for such services," and cites certain cases. If reliance is placed upon the technical corporate duties prescribed by the by-laws for the president, secretary and treasurer, we have already pointed out that both Messrs. Miller and Ballagh were appointed by the directors as General Manager and Sales Manager, whose duties are not prescribed anywhere but it was generally understood by all the directors and parties interested to comprehend and include the development of devices and inventions.

Appellant's language just quoted is neither a correct nor accurate statement of the law. The rule is stated in Fletcher on Corporations, Perm. Ed., Vol. 5, Sec. 2114, p. 387 in heavy type, as follows:

> "By the great weight of authority, if directors or other officers render unusual or extraordinary services for their company, not within the line of their ordinary duties, the circumstances may give rise to an implied promise for compensation under the general rules governing all implied contracts."

Numerous cases are cited from all the American states, as well as the Federal Courts, including the Supreme Court of the United States, to support this statement of the rule and the rule is the same in California.

In Section 2115 at page 393, it is said, quoting from *Hunter v. Conrad,* 230 N. Y. S. 202:

> "'. . . it is clear that a director of a corporation may lawfully be paid for services performed beyond the ordinary duties of a director.'"

and the section proceeds to give illustrations of such extraordinary duties. For example, where a director happens to be an attorney who performs professional services for the corporation or acted as its general counsel, or where a director acts as general manager and superintendent of construction. or used exceptional and extraordinary efforts in selling corporate stock, or performed manual labor outside of his duties as a director, or was an expert bookkeeper and auditor and furnished services of that character, or one who acts as an arbitrator in settling a dispute to which the corporation is a party, or acts as an agent or broker in procuring patents to land, or in obtaining loans, or in securing rights of way for a railroad, or acts as captain of a boat

owned by the corporation, an implied contract arises that the corporation becomes indebted to him for such services.

Taussig v. St. Louis & K. R. Co. (Mo. Sup. Ct.), 65 S. W. 936;

Fox v. Arctic Placer Min. & Mil. Co. (N. Y.), 128 N. E. 154. [See Appendix p. 23];

Jackson v. New York Central R. Co., 58 N. Y. 623;

Watts v. West Virginia Southern R. Co. (W. Va.), 37 S. E. 700;

Spence v. Sturgis Steel Go-Cart Co. (Mich.), 186 N. W. 393;

Lofland v. Cahall (Del.), 118 Atl. 1;

Pratt v. Wilcox (Wash.), 203 Pac. 949;

Paine v. Kentucky Refining Co. (Ky.), 167 S. W. 375;

Santa Clara Min. Ass'n. v. Meredith (Md.), 49 Md. 389, 33 Am. Rep. 264;

Cheeney v. Lafayette B. & M. R. Co. (Ill.), 68 Ill. 570, 18 Am. Rep. 264;

Rogers v. Hastings & Dakota Ry. Co., 22 Minn. 25;

Ten Eyck v. Pontiac, O. & P. A. R. Co. (Mich.), 41 N. W. 905, 3 L. R. A. 378, 16 Am. St. Rep. 633;

Loewer v. Tonoke Rice Mill Co. (Ark.), 161 S. W. 1042;

New Orleans, B. R. & B. S. Packet Co. v. Brown, 36 La. 138, 51 Am. Rep. 5;

Spalding v. Enid Cemetery Ass'n. (Okla.), 184 Pac. 579. [See Appendix p. 23];

Waters v. American Finance Co. (Md.), 62 Atl. 357. [See Appendix p. 25];

Fitzgerald & Mallory Const. Co. v. Fitzgerald, 137 U. S. 100, 34 L. Ed. 608. [See Appendix p. 26];

Gumaer v. Cripple Creek Tunnel, etc. Co. (Colo.), 90 Pac. 81. [See Appendix p. 27.]

This is the rule announced and followed by this Court in

Montana Tonopah Mining Co. v. Dunlap (C. C. A. 9th), 196 Fed. 612. [See Appendix p. 29.]

This Court again followed the same rule in

Denman v. Richardson (C. C. A. 9th), 292 Fed. 19. [See Appendix p. 31.]

The rule is the same in California.

Zellerbach v. Allenberg, 99 Cal. 57, 33 Pac. 786. [See Appendix p. 33];

Bassett v. Fairchild, 132 Cal. 637, 52 L. R. A. 611, 64 Pac. 1082. [See Appendix p. 34];

King v. Grass Valley Gold Mines Co., 205 Cal. 698, 272 Pac. 290.

In the latter case plaintiff corporate officer claimed to have rendered services and to be entitled to compensation therefor as a mining engineer, mine manager and superintendent and was permitted to recover on the theory of *quantum meruit.* [See Appendix p. 39.]

See also:

San Leandro Canning Co. Inc. v. Perillo, 84 Cal. App. 635. [See Appendix p. 39.]

The first case cited by appellant to support its misstatement of the rule is

Finch v. Warrior Cement Corp. (Del.), 141 Atl. 54.

On the point under consideration the only question involved was whether, where a promoter submitting a plan to organize a new corporation to take over the assets of the present corporation, proposed to actively assist in the sale of bonds and in forming a syndicate therefor, the commissions which he received while acting as a director of the corporation for the sale of its bonds were illegally paid and must be returned. The commissions taken by the defendant directors were ten per cent of certain stock sales. The court says:

> "It will not do to say that the ten percent. flotation charge was a reasonable one. The question is, Was it the best that could reasonably have been obtained? It is manifest that, to the extent of the commission paid to Deer and Steward (defendant directors), the brokers were content to take less than the specified ten per cent."

In other words it was specifically found that the defendant directors received more for their services than would have been charged by others and further, "but aside from that, the services rendered in this case do not appear to have required the exertion of any more exceptional or extraordinary efforts than did the services rendered in the Lofland case"

Jones v. Foster (C. C. A. 4th), 70 Fed. (2d) 200, next cited, has not, so far as we can see, any possible application in its effect to the case at bar. The case was tried in the court below to a jury and the trial judge specifically instructed that the claimed "services performed were clearly not outside the scope of the duties pertaining to the defendant's office as a president of the corporation in accordance with the by-laws." [See Appendix p. 41.]

O'Leary v. Seemann (Colo.), 232 Pac. 667,

was a suit to compel the president and general manager of the corporation to account for the proceeds of a large amount of corporate stock which he had sold. It does not in any way depart from the correct rule as above stated but on its facts is entirely inapplicable to the case at bar. [See Appendix p. 18.]

We submit without comment that

Pindell v. Conlon Corp. (Ill.), 24 N. E. (2d) 882,

has no possible application to the case at bar. [See Appendix p. 41.]

Appellant cites

Larkin v. Enright, 37 N. E. (2d) 905,

an opinion by the Illinois intermediate Appellate Court. This was a suit to restrain defendant from voting two shares of stock, to restrain directors elected by the vote of these two shares from participating in the voting at any meeting of the board, to restrain the collection of certain money owing to the corporation and for other equitable relief. [See Appendix p. 42.]

Similarily under this sub-heading appellant cites

In re Dr. Voorhees Awning Hood Co. (D. C. Pa.), 187 Fed. 611.

This was a proceeding in bankruptcy in connection with which the president of the bankrupt corporation appears to have filed claims against it for salary and other compensation. We can see no possible connection between this case and the one at bar where officers have been paid compensation for services rendered pursuant to due and legal authorization by the board of directors. [See Appendix p. 43.]

It remains perhaps to establish that the devices and inventions developed by Messrs. Miller and Ballagh originated under circumstances which constituted them their individual property both as to the element of use or so-called "shop rights" and also from the proprietary standpoint and that, in conferring their free use upon the corporation and in assigning their present and future proprietary interest thereto, they were parting with property rights of value.

The authorities seem uniform that, prior to the assignment of patents or patent applications or interests, title to the patents or patent rights are in the individual defendants where the contract of employment does not provide otherwise.

U. S. v. Dubilier Corp., 289 U. S. 178, 77 L. Ed. 1114. [See Appendix p. 43];

Dysart v. Remington Rand Inc. (D. C. Conn.), 40 Fed. Supp. 596;

Geer Grinding Mach. Co. v. Stuber (Mich.), 276 N. W. 514;

White Heat Products Co. v. Thomas (Pa.), 109 Atl. 685;

Dean v. Hodge (Minn.), 27 N. W. 917. [See Appendix p. 46];

Heywood-Wakefield Co. v. Small (C. C. A. 1st), 87 Fed. (2d) 716. [See Appendix p. 49.]

"(c) *The Inventions of the Defendants cannot be classified as Services.*"

Appellant's argument under this heading is hardly worthy of an answer, and we shall certainly devote but little space to that purpose. Appellant could hardly deny that the royalties paid by defendant corporation to plaintiff from the years 1928 through 1939 totalling $101,406.61 [Pl. Ex. 18-D] did not have a current value year

by year to plaintiff. If defendant officers had retained their proprietary rights in the patents and devices which they developed for the company beginning about 1939, and the company had been obliged to pay royalties upon them, obviously this would have constituted a charge against the company's revenues. However, the individual defendants devised these inventions with the sole idea and for the sole purpose of improving the company's business and making it the beneficiary in so far as their royalty free use was concerned, and, in addition thereto, conferred the proprietary ownership upon the company. If this does not constitute the rendition of "services" we do not understand the meaning of that term and, in our opinion, this argument of appellant characterizes and should discredit its case *in toto*.

"(d) *Even if the Inventions of the Defendants should be considered, they were not of sufficient Value to support the amount of the Salaries.*"

Appellant introduces its argument here by stating that this is an equity case and that the appellate court has the power to review the facts, decide them *de novo*, and overrule the findings of fact made by the trial court. We have already, at too great length no doubt, replied to these contentions.

The record shows the steady and progressive increase in the sales of the inventions and devices year by year from the time they were first manufactured, amounting, generally speaking, to more than a doubling in each successive year. We have detailed the testimony for defendants relative to the value, actual and potential, of these inventions and devices to the corporation. The only testimony *contra* offered by plaintiff was that of the witness Grant [R. 543-548] and its employee, Chestnut [R. 425-427, 565], both called in rebuttal on

this point. A reading of their testimony demonstrates its worthlessness and self-serving character. The trial court had the benefit of seeing and hearing both of these gentlemen as it did the witnesses for the respondents on this issue. On the record as made, we are confident that this Court will not disturb the findings of the trial court on this issue irrespective of whether it has the reviewing power to do so or not, which we maintain it does not have.

"Defendants' Salaries were part of the Conspiracy on the part of Defendants to fraudulently enrich themselves at the Expense of Plaintiff, the minority Stockholders."

Here again, just as in its complaint, appellant makes an *assertion* of "fraudulent conspiracy." The mere bald assertion, however, is all that it offers on the point. The record is devoid of any evidence to support it.

There were many reasons, from the standpoint of a wise and conservative business policy, why defendant corporation stopped paying dividends when it did. These reasons appear in the record as evidence produced by defendants as against a total lack of any evidence on the point produced by plaintiff. The court will undoubtedly take notice of the fact that at the beginning of 1939 all business was faced with uncertainty. Those operating to any extent in the export trade and, even more, those manufacturing items made of rubber, as was this company, might be considered to have been facing more than an uncertainty. Certain fortunate subsequent developments as to the rubber situation were purely fortuitous and could not have been foreseen at that time. The matter of dividends was discussed at a directors' meeting on November 29, 1940 at which time Dulin offered his opinion that the company was in a position to declare and pay a dividend. Naturally, as president of the plain-

tiff, he desired it to participate further in the "gravy" it had been enjoying from defendant company for years. Directors Ballagh and Miller, however, were of the opinion that no dividend should be declared at that time in view of the company's requirements for accumulating a rubber reserve, intended plant expansion, "the requirement of paying royalties on protectors manufactured and sold and the validity of the patents on its manual and hydraulic applicators" [R. 255, 256]. Defendant Ballagh gives as one of Mr. Miller's reasons for suspending dividends the necessity of creating a reserve against the litigation instituted by plaintiff for royalty on the Bettis-Hopkins patent licensing agreement and, as his own reasons, the critical war situation, contemplated expansion, attempts to get into war work, and inadequate cash on hand [R. 361]. Mr. Miller states that he was responsible for suspending dividends [R. 382] and his reasons therefor were contemplated plant expansion (two lots had actually been purchased), the war situation, the necessity of conserving capital, the fact that the company operated on a cash basis without the use of credit, and the Byron-Jackson royalty suit [R. 383].

All of these reasons were substantial and valid. They appealed to four out of five directors as being so and the Board acted upon them as a Board. The only dissenting director was plaintiff's president, Dulin, who obviously had a palpably direct personal interest in conflict with the best interests of the corporation of which he was, in name, a director.

The decision by the Board of Directors as to dividends was one of corporate policy purely within its jurisdiction and, in the absence of fraud, of which there is no scintilla of evidence in the case, neither this nor any other court can interfere with this determination of policy by the directors. The authorities which we have heretofore cited and quoted from, are uniform on this subject.

Ratification and Waiver.

In paragraph 21 at page 12 of its brief an assertion is made that Miller was overpaid in 1940 in the sum of $7750.00. The facts are that in 1940 (Dec. 1, 1939 to Dec. 1, 1940) he received a total compensation of $19,252.00. At the directors' meeting of March 18, 1940 he was voted an annual salary of $1,500 per month commencing March 1, 1940, Director Dulin being present and voting therefor. Whatever may be the law elsewhere, in California transactions between a corporation and its directors are neither void nor voidable if the fact of a beneficial interest to the director involved therein is disclosed to or known by the shareholders and they ratify the transaction in good faith by a majority of those entitled to vote. (Civil Code, Sec. 311 (b).)

Thus, in the absence of actual fraud, the various ratifications at the stockholders' meetings in the case at bar are controlling. See:

Russell v. Patterson (Pa.), 81 Atl. 136;

Middletown v. Arastraville Min. Co., 146 Cal. 219.

In the latter case the court announced the general rule that *stockholders occupy no such fiduciary relationship to each other as to preclude a stockholder from voting at a stockholders' meeting upon any question in which he has an individual interest adverse to the other stockholders.* [See Appendix p. 52.]

All actions of the Board of Directors for the years 1939 and 1940 were ratified at the subsequent annual meetings of the stockholders by a vote of three-quarters of the outstanding stock [R. 232, 234, 261-265], excepting that, for the year 1941, the record does not show the proceedings of the annual stockholders' meeting at the conclusion of that year since this suit was instituted before its termination.

At the annual stockholders' meeting on January 21, 1941 [R. 261] Dulin, with full knowledge previously acquired at directors' meetings of his fellow-directors' ideas as to the worth of the services of Messrs. Miller and Ballagh, seconded a motion electing the same directors for the ensuing year and voted in favor of it. At the directors' meeting of the same date [R. 267], Dulin voted for the re-election of the same officers, which vote, by every fair implication, carried with it an approval of their compensation at the current rate and a waiver of any objections thereto. Dulin was absent at both the stockholders' and directors' meetings held on January 16, 1940 at the end of the fiscal year 1939 though he had received due notice thereof [R. 232-238]. Dulin knew the attitude of the directors on the compensation question and if he did not agree with them, it was his duty to propose other directors and officers at both the stockholders' and directors' meetings which he attended. Similar action has been condemned and held to be a ratification and waiver in

Klein v. Independent Brewing Assn. (Ill.), 83 N. E. 434. [See Appendix p. 52], and

Nahikian v. Mattingly (Mich.), 251 N. W. 421.

Under these circumstances we submit that plaintiff is in no position to complain as it does here.*

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*In a footnote at page 6 of its brief appellant states that defendant Miller received $19,252 for 1940 and $13,500 for 1941 up to September 10. Nothing is said as to 1939 nor could it well be since Miller's compensation in that year was authorized and voted for by director Dulin, plaintiff's representative [R. 213]. At the directors' meeting of March 18, 1940 [R. 240] Dulin approved and voted for an increase for Miller from $1,000 to $1,500 per month commencing March 1st. From December 1, 1939, the beginning of the fiscal year, to March 1, 1940 Miller received $3,000, or $1,000 per month which compensation Dulin had previously voted for and approved [R. 214]. From March 1, 1940 to December 1, 1940 Dulin had voted for and approved Miller's compensation in the sum of $13,500, or at the rate of $1,500 per month, or a total of $16,500 for the twelve months. Miller actually received $19,252 for the twelve months because he was voted a bonus equal to two months' pay at a directors' meeting at which Dulin was absent [R. 252]. For the period from December 1, 1940, to September 10, 1941, Miller received $14,000, being the exact amount authorized by the board for that period with the approval and affirmative vote of Dulin. Consequently for the whole period from December 1, 1939, to September 1, 1941, the amount received by him in excess of Dulin's own authorization and vote is only $2,752 and not $7,750 as claimed by appellant and stated in the footnote, text and complaint.

Conclusion.

It is unfortunate that the record in this case cannot and does not portray the subsequently demonstrated wisdom of the policy adopted by defendant company's directors in investing money, time and effort, the latter being supplied by the individual defendants Miller and Ballagh, inventing and devising new articles of manufacture and sale and in placing them on the market to supplant the serious loss in business necessarily resulting from the invalidation of the Bettis patent. If the court were at all in doubt as to the wisdom and good faith of the directors in adopting the policy which they honestly did for the welfare of the corporation, it might well remand the case to the District Court for the purpose of supplementing the record by bringing the company's history up to date.

Notwithstanding that this is purely an action at law, the equities are all with the respondents. Appellant purchased one-quarter of the total capital stock of the respondent company in September, 1928, paying therefor a total of $25,000 [R. 61]. Since that time and up to the end of 1939 it has realized a total of $221,906.61 in cash on that investment or almost one hundred per cent a year [Pl. Ex. 18-D]. Plaintiff has rendered no services whatever nor anything useful of any kind to defendant company since the failure of the Bettis patent in 1932. It still, however, desires large dividends and also royalty payments on the invalidated patent, and its "representative" Dulin sits on the company's Board of Directors, apparently for the sole purpose of obtaining dividends and royalty payments for the benefit of the plaintiff of which he is president. If this were, indeed, a suit in equity, we suggest that plaintiff's position and the conduct of its "representative" on defendant corporation's Board is hardly one which would commend itself to a court of

equity. It complains because of compensation paid to company employees and officers who are rendering invaluable service to the company and, in fact, enabling it to survive, the admitted reason for the complaint being a temporary cessation of dividends to itself on an investment for which it has been repaid nearly ten times over.

The trial Court made findings of fact and conclusions of law in no uncertain terms. It found specifically that the individual defendants did not in any way dominate the Board of Directors [R. 62]; that both individual defendants have "at all times * * * discharged their duties as such officers faithfully, efficiently, conscientiously, loyally and meritoriously" [R. 63]; that the services rendered by Messrs. Ballagh and Miller "are now and will continue to be a very great value to said corporation"; that as to each of them the compensation for the period involved "was fair, just and reasonable as to defendant Patterson-Ballagh Corporation at the various times it was authorized, approved and paid," [R. 64-67], and in no case did either Mr. Miller or Mr. Ballagh vote upon a resolution affecting his own compensation [R. 64-67].

On this record it is clear:

(1) That there is no proof of fraud, conspiracy or other tortious act, and that the evidence compels a finding otherwise.

(2) That there is no proof that the compensation paid the individual defendants was either unfair or unreasonable. The evidence compels the conclusion that it was fair and reasonable and that the corporation obtained value received therefor.

(3) That, in the absence of fraud, the Court has no visitorial powers to interfere with determinations of

policy by a corporate board within the sphere of its jurisdiction.

(4) That plaintiff has no standing to complain in equity if this be regarded as a suit in equity.

(5) That if it be regarded as an action at law, plaintiff has wholly failed to prove its case as alleged in its complaint by a preponderance of the evidence or otherwise.

For all the reasons foregoing, we respectfully submit that the Findings, Conclusions and Judgment of the trial court should be affirmed.

Respectfully submitted,

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APPENDIX.

For the convenience of the Court and in conformity with Rule 20(f) we quote hereafter pertinent excerpts from cases cited in the brief, under appropriate headings.

Scope of the Reviewing Powers of the Circuit Court of Appeals on This Appeal.

EXCERPTS FROM CASES CITED ON PAGE 9 AS TO LIMITATIONS UPON THE APPELLATE COURT.

Cherry-Burrell Co. v. Thatcher (C. C. A. Mont., 9th Cir., 1940), 107 F. (2d) 65 (Br. p. 9):

> "This is simply a case of a conflict in the evidence, and the court below reached its conclusion by determining the weight of the evidence and the credibility of witnesses. Giving due regard 'to the opportunity of the trial court to judge of the credibility of the witnesses' as we are required to do, Federal Rules of Civil Procedure, Rule 52(a), 28 U. S. C. A. following section 723c, we cannot say that the findings are 'clearly erroneous.' We cannot, therefore, set aside the findings."

Storley v. Armour & Co. (C. C. A. 8th, 1940), 107 F. (2d) 499 (Br. p. 9):

> "It is unnecessary to set out the evidence in detail, since it is elementary that a finding by a trier of the facts based upon conflicting evidence will not be disturbed by an appellate court. H. H. Cross Co. v. Simmons, 8 Cir., 96 F. 2d 482, 486; Crowell v. Baker Oil Tools, 9 Cir., 99 F. 2d 574, 577."

Crowell v. Baker Oil Tools Inc. (C. C. A. 9th), 99 F. (2d) 574 (Br. p. 9):

"Appellant contends that he granted the license to appellee by mistake, because he gave his consent, or granted the license, on the understanding that appellee was granting him a license to use ball valves; that therefore he had rescinded the license granted appellee pursuant to the above quoted statute, and the court below could not bring it into being again. This contention is based on the premise that appellant gave his consent by mistake. The trial court found to the contrary. Although appellant's testimony supports his contention. Mellin's testimony is contrary. *In view of the conflict, we believe the trial court made no 'serious or important mistake' and that its finding was not 'clearly erroneous.'* Furrer v. Ferris, 145 U. S. 132, 134, 12 S. Ct. 821, 36 L. Ed. 649; National Reserve Ins. Co. v. Scudder, 9 Cir., 71 F. (2d) 884; Collins v. Finley, 9 Cir., 65 F. 2d 625, 626; United States v. McGowan, 9 Cir., 62 F. 2d 955, 957, affirmed 290 U. S. 592, 54 S. Ct. 95, 78 L. Ed. 522; Clements v. Coppin, 9 Cir., 61 F. 2d 552, 558; Exchange National Bank v. Meikle, 9 Cir., 61 F. 2d 176, 179; Jones v. Jones, 9 Cir., 35 F. 2d 943, 945; Easton v. Brant, 9 Cir., 19 F. 2d 857, 859; Gila Water Co. v. International Finance Corporation, 9 Cir., 13 F. 2d 1, 2; Rules of Civil Procedure, rule 52(a), 28 U. S. C. A. following section 723c.

"It is also contended that the license granted appellee by appellant was rescinded on the further ground that appellant's consent was obtained by Mellin's fraud. *We think the trial court's finding to the contrary must be sustained, because the evidence, at most, was conflicting only.*" (Italics ours.)

State Farm Mut. Automobile Ins. Co. v. Bonacci, 111 Fed. (2d) 412 (Br. p. 9):

> "The facts largely relied upon in this case consist of testimony and written statements given or made by the defendants not in the presence of the lower court but in the course of the trial of the damage actions in the state court. The lower court, as to such evidence, had no better opportunity of judging the credibility of the witnesses than does the appellate court."

The opinion of Judge O'Brien proceeds (Br. p. 15):

> "The same principle has been accepted in this State in Holmes v. Camp, 180 App. Div. 409, 412, 167 N. Y. S. 840. In an action for damage to property the six-year statute applies *even in those instances where the alleged remedy may be equitable in form.* Keys v. Leopold, 241 N. Y. 189, 192, 149 N. E. 828." (Italics ours.)

EXCERPTS FROM CASES CITED ON WHETHER THE ACTION IS ONE AT LAW OR IN EQUITY. (Br. pp. 15-18.)

Cwerdinski v. Bent, 11 N. Y. Supp. (2d) 208 (Br. p. 15):

> "The purpose of the first cause of action is to compel the parties who were the recipients of the bonus to return to the corporation the difference between the sums actually received by them and the amounts which should have been paid under the bonus plan. In short, the first cause of action involves sums of money which these appellants, and other individual defendants, are said to have received wrongfully from the New Jersey Corporation. Since that is so, the corporation could have instituted an

action for money had and received, and consequently no accounting would have been necessary. Had the corporation brought the action the six-year statute of limitations would have controlled. A shareholder is in no better position than the corporation, even though the complaint is addressed to the equity side of the court."

Wallace v. Lincoln Savings Bank (Tenn.), 15 S. W. 448, 24 Am. St. Rep. 625 (Br. p. 16):

> " 'This kind of suit is. at last, but the suit of the corporation for its benefit and upon its right of action. If for any reason the corporation is estopped from suing, or its action is barred, the suit by the stockholder or creditor is likewise affected,' "

In the course of his opinion Judge Lurton quotes with approval an excerpt from Morawetz on Corporations, as follows:

> " 'A suit of this character is brought to enforce the corporate or collective rights, and not the individual rights of the shareholders. It may therefore properly be regarded as a suit brought on behalf of the corporation, and the shareholder can enforce only such claims as the corporation itself could enforce. Moreover, the essential character of a cause of action belonging to a corporation remains the same, whether the suit to enforce it be brought by the corporation or by a share-holder. Thus a legal right of action would not be treated as an equitable one, or become governed by the rules applicable to equitable causes of action, as to limitations, etc., because a shareholder has brought suit in equity to enforce it on behalf of the company.' "

Becker v. Empire Power Co., 31 N. Y. S. (2d) 914 (Br. p. 16):

> "In other words, if the unconscionable and unlawful gains obtained by miscreant directors and officers are known to be in a fixed amount and do not exceed the correlated loss suffered by the corporation, then there is no occasion or necessity for resort to an equitable action for an accounting: the amount being known, an action at law for money had and received will lie and is the proper remedy. I so interpret Dunlop Sons, Inc. v. Spurr, 285 N. Y. 333, 336, 34 N. E. (2d) 344. In the case at bar the extent of the illegal gains of Phillips and Olmsted and consequent loss to the corporation was definitely known for paragraph VI of the complaint expressly alleges that they directed into their own pockets the sum of $7,385,075; that being a known fact, and the gains obtained by Phillips and Olmsted and the consequent loss to the corporation being the same in amount, there was no need, therefore, to sue for an accounting and there existed a full, adequate and complete remedy at law to sue for money had and received and the six-year statute would apply."

Dunlop v. Dunlop, 34 N. E. (2d) 344 (Br. p. 16):

> "Potter v. Walker, 276 N. Y. 15, 11 N. E. 2d 335, did not decide that the ten-year Statute of Limitations (Civil Practice Act, §53) is necessarily applicable to all cases in which corporate directors have profited in any degree through a breach of their fiduciary duties. In such a case an action for an accounting may be brought only for the recovery of gains received by the directors beyond the amount of losses caused to the corporation by their wrong. Where, as in the present case, the gains received

by the directors do not exceed the correlated losses suffered by the corporation, no accounting is necessary and the Statute of Limitations, Civil Practice Act, §48, which controls the remedy at law is to be applied. See Goldstein v. Tri-Continental Corporation, 282 N. Y. 21, 24 N. E. 2d 728."

Gormley v. Slicer (Ga. Sup. Ct.), 172 S. E. 23 (Br. p. 17):

Paragraphs 1 and 2 of the Supreme Court's opinion on certification read:

"1. The facts show essentially an action at law for damages based on tort, without any grounds for equitable relief." (Citing many cases.)

"2. The fact that it was alleged in the petition and in the motion to refer the case to the auditor and in the motion to recommit the case to the auditor, that the case was one in equity, and that the judge in deciding the case considered it was in equity and it was so recited in the bill of exceptions, considered in connection with other facts set forth in the second question propounded by the Court of Appeals, did not make the case one in equity. The second question propounded by the Court of Appeals is answered in the negative."

Potter v. Walker, 287 N. Y. S. 812 (Br. p. 17):

"The following principles appear to be established:

"First, that, as the right of the stockholder is derivative, the period of time within which he may sue is measured by the rule which would be applied if his corporation had brought the suit. Brinckerhoff v. Bostwick, *supra;* Pollitz v. Wabash R. Co.,

207 N. Y. 113, 100 N. E. 721; Curtis v. Connly, 257 U. S. 260, 42 S. Ct. 100, 66 L. Ed. 222.

"Second, that the directors of a corporation being held to the liability of trustees as to the care of corporate property may be sued in equity for an accounting for any dereliction of duty. Bosworth v. Allen, 168 N. Y. 157, 61 N. E. 163, 55 L. R. A. 751, 85 Am. St. Rep. 667; Asphalt Construction Co. v. Bouker, 150 App. Div. 691, 135 N. Y. S. 714, affirmed 210 N. Y. 643, 105 N. E. 1080. However, they are trustees of an implied or constructive, rather than an express, trust and therefore the jurisdiction of equity is concurrent and not exclusive. Pomeroy Eq. Juris (4th Ed.) §157.

"Third, that even where a suit in equity *for an accounting* is permissible if a legal as well as an equitable remedy exists as to the subject-matter of the suit, *the limitation, applicable to the legal remedy must be applied.* Kane v. Bloodgood, 7 Johns. Ch. 90, 11 Am. Dec. 417; Keys v. Leopold, *supra;* Dumbadze v. Lignante, *supra.*

"Fourth, that a corporation as distinguished from its stockholders may sue its directors at law *where only legal relief is sought.* O'Brien v. Fitzgerald, 143 N. Y. 377, 38 N. E. 371; Dykman v. Keeney, 154 N. Y. 483, 48 N. E. 894.

"In the light of these principles, considering the causes of action attacked, does it appear that as to the subject-matter of any of them the plaintiff had a legal as well as an equitable remedy?" (Italics ours.)

Emerson v. Gaither (Md.), 64 Atl. 26 (Br. p. 18):

"First. The authorities are not uniform as to how far a court of equity has jurisdiction in suits by corporations, or their receivers, against directors who were guilty of negligence or of acts contrary to some statutory provision. It cannot be denied that there may be charges of mismanagement or negligence, causing loss or injury to the corporation, for which there could be no reason for going into equity; the corporation having a complete and adequate remedy at law. In 3 Clark & Marshall on Cor., §755, it is said that 'the corporation may maintain an action at law against them at common law—an action on the case—to recover damages'; but those authors go on to say: 'Or it may maintain a suit in equity *when any special ground of equitable jurisdiction exists, as in a case where an accounting or discovery or injunction is necessary.*' Judge Thompson, in the article written by him on Corporations in 10 Cyc., thus speaks of the subject, on page 836: 'The proper remedy is said to be an action at law for damages, and not a bill in equity, where no accounting of the financial condition of the corporation is necessary to determine the extent of their liability. The jurisdiction of courts of equity to compel unfaithful directors to account to the corporation, or to its representative, for frauds and breaches of trust has been well established since the time of Lord Hardwicke, and unquestionably this is a proper forum in nearly all such cases, although this statement does not exclude the jurisdiction of courts of law in cases appropriate for the exercise of that jurisdiction; the two remedies being often concurrent.'" (Italics ours.)

Corsicana Nat. Bank v. Johnson (C. C. A. 5th), 218 Fed. 822 (Br. p. 18):

"The bill in this case charged the defendant, who had been an officer of the plaintiff bank, with liability for the loss sustained by the bank on a loan of its funds in an amount which exceeded one-tenth of the amount of the bank's paid-in capital and surplus, the ground of the asserted liability of the defendant being his alleged participation in and responsibility for the violation of the statutory prohibition of such a loan. 5 Fed. Stat. Ann. 139, 34 Stat. 451. The suit was the assertion of the right of the bank to hold the defendant liable in his personal and individual capacity for all damages sustained by the bank in consequence of the defendant knowingly violating the provision of the above-mentioned statute. Rev. Stat. U. S. §5239. Plainly a suit to recover damages so sustained may be maintained at law, *and is not cognizable by a court of equity, in the absence of any showing of the inadequacy of the legal remedy which is available.* Cockrill v. Cooper, 86 Fed. 7, 29 C. C. A. 529; Stephens v. Overstolz (C. C.), 43 Fed. 465.

"In the case at bar no fact was alleged or proved which tended to show any inadequacy of the legal remedy to which the plaintiff might have resorted. The plaintiff's claim was that it had lost the total amount loaned, less what had been and what might yet be realized from certain corporate stock which it had received in a settlement of the bankrupt estate of one of the insolvent borrowers. The holding of that stock by the plaintiff constituted no ground for a resort to a court of equity. The bank's claim was subject to be reduced by the amount already realized on that stock and by the reasonable value of it, if it still represents anything of value. This abatement

of the amount of damages recoverable could be made in a court of law as well as in a court of equity. It was simply a matter of showing the actual loss sustained by the plaintiff as a result of the forbidden loan. It was not made to appear that in a court of law there was any obstacle in the way of proving and recovering the damages sustained. In short, we discover no equitable feature in the claim sought to be enforced. *It was a simple legal demand for damages, to be assessed in a judgment for money.* The suit in equity could not properly be maintained because the case was one where a plain, adequate, and complete remedy may be had at law for the wrong complained of. Southern Pacific R. R. Co. v. United States, 200 U. S. 341, 26 Sup. Ct. 296, 50 L. Ed. 507; Smyth v. N. O. Canal & Banking Co., 141 U. S. 656, 12 Sup. Ct. 113, 35 L. Ed. 891." (Italics ours.)

EXCERPTS FROM CASES CITED ESTABLISHING THAT IN ANY EVENT THE BURDEN OF PROOF IS UPON PLAINTIFF.

Nahikian v. Mattingly (Mich.), 251 N. W. 421 (Br. p. 26):

"The fixing of the salary of defendant by the board of directors may have been ill-advised action. considering the financial condition of the corporation and the character of the services of the president, but it was a matter of corporate management, vested in the directors, and their action, *in the absence of fraud or willful or wanton departure from known or manifest duty, bars judicial substitution of opinion.*

"In McKey v. Swenson, 232 Mich. 505, 205 N. W. 583, we held action in fixing salaries wholly void and cast the burden upon the officers to give the court in-

formation upon which reasonable compensation could be fixed. Such, however, is not the case at bar, for here we do not have wholly void action *but only assertion of unreasonable compensation* and the burden is on plaintiff to establish the charge.

"As said in Burden v. Burden, 159 N. Y. 287, 54 N. E. 17, 23: 'The plaintiff is in the position of all minority stockholders, who cannot interfere with the management of the corporation so long as the trustees are acting honestly and within their discretionary powers.'

"A minority complaining stockholder, if he avers excessive salary, *must show facts establishing unjustifiable oppression in such respect.* The evidence fails to show that salary voted defendant, by the board of directors was so unreasonable or excessive, under the circumstances, as in itself to be deemed fraudulent and, therefore, authorizing restoration in whole or in part. We may not readjust the salary without a yardstick applicable to the particular circumstances and not even then upon mere difference of opinion from that of the board of directors, *but only upon concrete proof that the salary evidences wrongdoing or inexcusable oppression to the point of being fraudulent.* Less than this would constitute an intolerable interference with legitimate internal corporate management.

"It is a well-settled rule of law that the authority of the directors is absolute when they act within the law, and that questions of policy and internal management are, in the absence of nonfeasance, misfeasance, or malfeasance, left wholly to their decision. *Ratification by the board of directors of an increase in defendant's salary, if made in good faith and be-*

lieved to be for the best interest of the company, validated the increase. Decree as to salary reversed." (Italics ours.)

Chapman v. Troy Laundry Co. (Utah), 47 Pac. (2d) 1054 (Br. p. 26):

"If we assume that there was bad faith in the minds of the directors on the 8th, then it would seem to follow that they must have, for some reason, relied on Kilpatrick. But to assume the fact is to eliminate the necessity for proof. Our assumptions must be to the contrary until proof overcomes them."

Bodell v. General Gas & Elec. Corp. (Del.), 132 Atl. 442 (Br. p. 27):

"I do not understand the defendants to argue that the action of the directors in this particular is not reviewable. They do insist, however, that inasmuch as the matter of the issuance of the stock was placed by the certificate of incorporation in their control, the general principle which excludes stockholders from matters of management *and accords to the acts of the directors a presumption in favor of their propriety and fairness, is to be here applied. This is true.*" (Italics ours.)

Cole v. National Cash Credit Ass'n (Del.), 156 Atl. 183 (Br. p. 27):

"There is a presumption that the judgment of the governing body of a corporation, whether at the time it consists of directors or majority stockholders, is formed in good faith and inspired by a *bona fides* of purpose. Robinson v. Pittsburgh Oil Refining Corp., 14 Del. Ch. 193, 126 A. 46; Davis v. Louisville Gas & Electric Co., 16 Del. Ch. 157, 142 A. 654."

Karasik v. Pacific Eastern Corp. (Del.), 180 Atl. 604 (Br. p. 27):

> "There is a presumption, rebuttable of course, that the directors of a corporation are actuated in their conduct of the business of the corporation by a *bona fide* regard for the interests of the corporation. Mercantile Trading Corp. v. Rosenbaum Grain Corp., 17 Del. Ch. 325, 154 A. 457; Davis v. Louisville Gas & Electric Co., 16 Del. Ch. 157, 142 A. 654; Finch v. Warrier Cement Corp., 16 Del. Ch. 44, 141 A. 54; Robinson v. Pittsburgh Oil Refining Corp., 14 Del. Ch. 193, 126 A. 46. An honest mistake of business judgment on the part of directors is not reviewable by courts. This is the general rule and it is supported by the decision of the Supreme Court of this State in Bodell v. General Gas & Electric Corp., 15 Del. Ch. 420, 140 A. 264."

Anderson v. Bean (Mass.), 172 N. E. 647, 72 A. L. R. 959 (Br. p. 27):

> "The general principle is that stockholders have no individual interest in the profits of a corporation until a dividend has been declared, that the accumulation of a surplus does not of itself entitle stockholders to a dividend, that the time when a dividend shall be declared and its amount rest in the sound discretion of the corporation or its authorized officers, usually the board of directors, that the action of such officers will not be disturbed if taken in good faith according to law and not in plain violation of the rights of stockholders, and that rational presumptions will be indulged in favor of the honest, decision of such officers. Tax Commissioner v. Putnam, 227 Mass. 522, 537, 116 N. E. 904, L. R. A. 1917F, 806; Fernald v. Frank Ridlon Co., 246 Mass. 64, 71, 140 N.

E. 421; Nutter v. Andrews, 246 Mass. 224, 227, 142 N. E. 67; Lee v. Fisk, 222 Mass. 418, 421, 109 N. E. 833; Thomas v. Laconia Car Co., 251 Mass. 529, 535, 146 N. E. 775; Boston Safe Deposit & Trust Co. v. Commissioner of Corporations and Taxation, 262 Mass. 1, 5, 159 N. E. 536; Adams v. Eastern Massachusetts Street Railway, 257 Mass. 115, 131, 153 N. E. 466; Morse v. Boston & Maine Railroad, 263 Mass. 308, 311, 160 N. E. 894 67 A. L. R. 758. It is urged that the case at bar constitutes an exception to the general rule *because the trustee owning one-half the stock in his own right and one-half as trustee was in absolute control of the corporation* and was bound to do what a court of equity may think he ought to have done in way of declaration of dividends, and that to this end the corporate entity ought to be regarded as a fiction. This contention cannot be supported. The trustee acted in good faith." (Italics ours.)

Winberg v. Camp Taylor Dev. Co. (Ky.), 95 S. W. (2d) 261 (Br. p. 28):

"It does not devolve upon the officer or director whose compensation is in question to prove that the compensation is fair, but the objecting stockholder *must establish affirmatively* that the compensation is unreasonable, and these facts must be shown by the pleadings as well as the proof. Beha, *et al.* v. Martin, *et al.*, 161 Ky. 838, 171 S. W. 393." (Italics ours.)

Borg v. International Silver Co., 11 Fed. (2d) 147 (Br. p. 29):

"The Colt transaction may have been improper; we cannot try it here. The first proposed sale, which

was enjoined, we may assume to have been improper. Together we will not say that they throw no suspicion on the directors' motives. But suspicion is hardly enough, unless the balance of advantage weighs very strongly in the plaintiffs' favor."

Noel v. Parrott (C. C. A. 4th), 15 Fed. (2d) 669, cert. den. 47 S. Ct. 457, 273 U. S. 754, 71 L. Ed. 875 (Br. p. 29):

"It needs neither argument nor citation of authority to establish the proposition that the directors were without authority to give away the corporate assets, and that for them to make to several of their members and other persons a gift of a large sum of money from the corporate assets would be neither 'wise' nor 'proper,' and would amount to an illegal misapplication of corporate funds. *We must assume that the directors did not intend such a flagrant violation of their trust.* Delaware, L. & W. R. Co. v. Kutter (C. C. A. 2nd), 147 F. 51, 77 C. C. A. 315; Hobbs v. McLean, 117 U. S. 567, 6 S. Ct. 870, 29 L. Ed. 940; U. S. v. Cent. Pac. R. Co., 118 U. S. 235, 6 S. Ct. 1038, 30 L. Ed. 173." (Italics ours.)

Gray Corp. v. Meehan (C. C. A. 1st), 54 Fed. (2d) 223 (Br. p. 29):

"When acts are done by officers of a corporation apparently authorized to perform them, in the absence of a public statute or charter to the contrary, the presumption is in favor of their regularity. The burden is on those who claim the contrary to prove affirmatively otherwise."

Fornaseri v. Cosmosart Realty Etc. Corp., 96 Cal. App. 549 (Br. p. 30):

> "Every presumption is in favor of the good faith of the directors. Interference with such discretion is not warranted in doubtful cases. In *Gamble v Queens County Water Co.,* 123 N. Y. 91 (9 L. R. A. 527, 25 N. E. 201), it is said: 'To warrant interference by a court in favor of minority stockholders . . . a case must be made out which plainly shows that such action is so far opposed to the true interests of the corporation itself as to lead to the clear inference that no one thus acting could have been influenced by any honest desire to secure such interest, but that he must have acted with an intent to subserve some outside purpose, regardless of the consequences to the company.'"

Michaels v. Pacific Soft Water Laundry, et al., 104 Cal. App. 366 (Br. p. 31):

> "The general rule is that the testimony of a witness cannot be wholly disregarded, but that unless it is impeached or contradicted by other testimony, by some presumption, or by an inference deducible from the facts proved, or unless it is inherently improbable, the trial court must accept it as true. (10 Cal. Jur. 1143; *Stewart v. Silva,* 192 Cal. 405, 410 (221 Pac. 191), concurring opinion; *Sun-Maid Raisin Growers v. Papazian,* 74 Cal. App. 231, 239 (240 Pac. 47).) *This rule is particularly applicable to a case such as we have here where the issue is fraud or good faith.* The presumption against fraud, which approximates the presumption against crime (*Truett v. Onderdonk,* 120 Cal. 581, 588 (53 Pac. 26)), the presumption that private transactions have been fair and regular, and the presumption that the ordinary course of

business has been followed (sec. 1963, subds. 1, 19 and 20, Code Civ. Proc.) are all *evidence* of good faith of the bank in this particular, and a contrary finding cannot stand without some evidence rebutting them." (First italics ours.)

Clark v. Oceano Beach Resort Co., 106 Cal. App. 574 (Br. p. 31):

"At most the evidence raises a suspicion that one of the motives of the defendant Long was to gain control of the corporation."

On the question of presumptions and burden of proof, the court says:

"Whether an assessment shall be levied or the property of a corporation shall be sold to raise funds with which to meet its obligations is a question for the determination of the corporation and its officers and not for the courts. 'It will be presumed that assessment were made in good faith and for a proper purpose. And if the purpose is a proper one the motive of the directors in levying it is immaterial.' (Fletcher's Cyclopedia of Corporations, sec. 4273.)"

EXCERPTS FROM CASES CITED BY APPELLANT ON THE ISSUE OF BURDEN OF PROOF.

Booth v. Beattie (N. J.), 118 Atl. 257 (Br. p. 35):

"The two managing directors have not been overpaid. In my judgment their services to the company since the adoption of the resolution were worth at least what they received. The company could, no doubt, hire managers at less pay, much less, but not managers who could produce results as these did. *They could be replaced, but not duplicated.* They are not merely carpet men, but Beattie carpet men, skilled

and trained to make and market Beattie rugs—a distinctive line in the trade and at the top." (Italics ours.)

Sotter v. Coatesville Boiler Works, et al. (Pa.) 101 Atl. 744 (Br. p. 35):

"If courts may depart at will from the rule just stated, and substitute their judgments for the legally exercised discretion of the directors of private business corporations, in determining the question of future compensation to be paid to the latter's employees, then there is no reasonable limit to the right of judicial interference with corporate management; but, fortunately, this is not the law."

Church v. Harnit, 35 Fed. (2d) 499 (Br. p. 40):

"As to the allowances made to Harnit by a board of directors, of whom three may be said to have been collaterally interested adversely to the corporation in that they themselves were to receive an allowance of bonus from Harnit, this does not wholly invalidate the action of the board. As directors, these three occupied a fiduciary relation toward the minority stockholders. Their action was open to the most careful scrutiny by the court. The burden is on them and upon Harnit to show that the contract was fair, honest, and reasonable in all respects, and especially with reference to the rights of the minority."

O'Leary v. Seemann (Colo.), 232 Pac. 667 (Br. pp. 42, 71):

"Counsel for Seemann claimed that services outside the regular duties of an officer give rise to a right of action for *quantum meruit.* We think that is so when there is a request to him to do the work or its equivalent (Mining & Milling Co. v. Prentice,

25 Colo. 4, 52 P. 210; Brown v. Silver Mines, 17 Colo. 421, 30 P. 66, 16 L. R. A. 426; Cheeney v. Lafayette, etc., R. W. Co., 68 Ill. 570, 575, 18 Am. Rep. 584; Corinne, etc., Co. v. Toponce, 152 U. S. 405, 14 S. Ct. 632, 38 L. Ed. 493); otherwise not. If it could be done without a request, any officer could involve a company to any extent of his own free will. *Since the resolution is not shown to have been passed, there is no request, and there is no subsequent vote,* as in Gumaer v. Cripple Creek, etc. Mining Co., 40 Colo. 1, 90 P. 81, 122 Am. St. Rep. 1024, 13 Ann. Cas. 781. But aside from that there is no showing of the value of the services of the defendant Seemann in selling the stock. This is for him to show. If the showing had been made, it is possible that the retention of the fruits of his services would have amounted to an implied contract as in Waters v. American Finance Co., 102 Md. 212, 62 A. 357." (Italics ours.)

Raynolds v. Diamond Mills Paper Co. (N. J.), 60 Atl. (Br. p. 58):

"But my conclusion is that no case is presented under the general equity power of the court, in which an equity judge should intervene and direct the distribution of profits in the form of dividends to these stockholders, setting aside the action for determination of the board of directors."

The court further said:

"As I recall it the fifth director, Mr. Raynolds, never qualified and the fourth director is a mere dummy, holding one share of stock in order to qualify. Messrs. Thompson, Van Gilder and Ralph Thompson, therefore, as a board of directors or con-

trolling the board of directors, *have fixed their salaries themselves at the sums that I have mentioned.*" (Italics ours.)

Article 3, Section 1, of the by-laws of Patterson-Ballagh Corporation, the heading whereof is "Officers and their duties" reads in part (Br. p. 59):

"The officers of this corporation shall be chosen by the directors and shall consist of a president, vice-president, secretary, treasurer, and such other officers as may be required by law or may be created by the board of directors."

Lillard v. Oil Paint & Drug Co. (N. J.), 56 Atl. 254 (Br. p. 63):

"Defendant's claim that the salary of $18,000 is reasonable and fair, although the same services had been previously rendered to the company for about half that sum, is based mainly on the contention that the defendant, at the time of assuming the management, was making as much or more in other business, and the conclusiveness of the previous smaller salary paid is answered, or attempted to be answered, by the contention that the profits received by Lillard, through the receipts of which he paid for his stock, should be taken as really salary paid to him. Neither of these contentions is sound."

Excerpt From Argument Presented in the Trial Court. (Br. p. 65.)

"When Mr. Dulin stated in his letter of March 27, 1940, that, on the basis of $232,000 of sales, $36,000 of combined executive salaries were all the business could stand, he did not include in said salaries any compensation for any inventions assigned to or used by the corporation royalty free.

"In 1940 Mr. Miller received a total compensation of $19,750. Mr. Dulin voted for the resolution awarding $18,000 of this compensation. In addition in his letter of March 27, 1940, Mr. Dulin states in substance that on the basis of $232,000 of sales $18,000 per year for Mr. Miller is not too much. Actually in 1940 the gross sales amounted to approximately $329,600, and the net sales to approximately $300,800. In 1941 Mr. Miller received compensation at the rate of $1,500 per month, and the gross sales in that year amounted to approximately $366,400 and the net sales to approximately $338,000. Consequently, even without considering the value of any of Mr. Miller's inventions which have been assigned to and used by the corporation royalty free, Mr. Miller's compensation cannot be said to be excessive. The fact that Mr. Miller during the period of time in question has assigned to the corporation, royalty free, two wire line wiper patents obtained in the United States, the Canadian patent on the open hole tool joint protector, the United States patent application on the open hole tool joint protector in respect to which two claims have been allowed, and all rights in respect to the remaining inventions would indicate that under no circumstances can it be said that Mr. Miller's compensation has been excessive. In fact on the basis of Mr. Dulin's letter of March 27, 1940, Mr. Miller has been underpaid.

"In considering the compensation paid to Mr. Ballagh, it is apparent from the evidence that Mr. Ballagh's services to the corporation have been of greater benefit to the corporation than those of Mr. Miller. If the corporation were required to pay a royalty of twenty-five cents on every protector installed by the hydraulic method (such as would be required under the Bettis cross-license agreement in the

event that the defendant corporation used the Bettis method), and similarly if the defendant corporation were required to pay reasonable royalties on lip protectors and pipe wipers, it would have paid out much more than has now been paid in the form of compensation. In addition the corporation would be a mere licensee and would not be the owner of the patents, a factor which is of great importance to the corporation and which places it in a position to make full use of the patent involved. Mr. Patterson, who was Mr. Miller's predecessor, had on various occasions engaged in inventive activities but had never given the corporation the benefit of the same [Tr. 163, 276-7]. The present policy of the corporation in taking assignments of any such inventions, royalty free, and of basing, in part, the compensation paid upon the proven value of such inventions has been determined upon by the board as the best business policy for the corporation to pursue, and it would appear that such an arrangement is much more advantageous to the corporation than any license agreement could be, whereby the corporation would not acquire title to the patent, and yet would be bound by an inflexible arrangement for many years to come.

"As to the law on the patents existing in this case and on those patents anticipated as the result of the inventions involved in this case, it is certain that prior to the assignments of such patents or patent applications, title to the patents or patent rights was in the individual defendants."

EXCERPTS FROM CASES CITED AT PAGES 68-69 OF BRIEF ON THE QUESTION OF AN IMPLIED CONTRACT REQUIRING A CORPORATION TO PAY THE REASONABLE VALUE OF SERVICES RENDERED BY ITS OFFICERS, AND ON THE QUANTUM MERUIT THEORY.

Fox v. Arctic Placer Min. & Mil. Co. (N. Y.), 128 N. E. 154 (Br. p. 68):

> "It is well-settled rule that directors and officers of a corporation serve without compensation for performing the usual and ordinary duties of their offices, unless an express provision is made therefor either by statute, charter, by-laws, or agreement. The question to be considered here, therefore, is whether the services rendered were outside the official duties of the plaintiff, and, if this be true, the rule is qualified.
>
> "The basis of a recovery for personal services must, of course, be a contract, and this must either be proven or implied. If the contract be not expressed, *it may be implied from the mere rendition and acceptance of the service.* Then the presumption is created that such services were to be compensated, because no one is expected to labor without hire. Barney v. Fuller, 133 N. Y. 605, 30 N. E. 1007." (Italics ours.)

Spalding v. Enid Cemetery Ass'n. (Okla.), 184 Pac. 579 (Br. p. 68):

> "As to the questions of law involved, counsel for both parties agree that the general rule is correctly stated in Fields v. Victor Building & Loan Co., 175 Pac. 529, as follows:
>
> "'A president and general manager of a corporation cannot maintain an action based on a *quantum*

meruit for past services rendered as president and manager, when no compensation for such services is provided in the charter or by-laws, and no compensation is fixed by any valid resolution passed prior to the rendition of such services, providing for compensation for such services.'

"But counsel for defendant contends that the case at bar is not governed by the general rule, but falls within one of the well-established exceptions thereto found stated in 2 Thompson on Corporations, §1736. Counsel for plaintiff do not notice this contention in their brief, apparently relying for success upon the authority of Fields v. Victor B. & L. Co., *supra.* So in its last analysis the real question is whether the case is governed by the general rule, or does it fall within one of the recognized exceptions thereto? We are of the opinion that the case falls within the exceptions mentioned by Mr. Thompson and the other authorities relied on by counsel for the defendant in his brief. Mr. Thompson, in the section of his work just referred to, says:

" 'There is a class of cases which, relaxing in some respects the rigid rule of the earlier cases, and establishing what may, perhaps, be called the modern doctrine of compensation, hold that the officers of a corporation may, under certain circumstances, recover compensation for their services within the line of their duties, on a *quantum meruit* or an implied promise to pay therefor; that where there is no prior express request, but where the services are rendered under such circumstances as to imply a promise, then the officer may recover. The presumption that the services were gratuitous *may be overcome by slight evidence.*' " (Italics ours.)

"Among the cases cited by the learned author in support of the text in Nat. L. & I. Co. v. Rockland, 36 C. C. A. 370, 94 Fed. 335, where he says (and we agree with him)—

" 'The rule was fully and admirably stated by a federal court thus: "A thoughtful and deliberate consideration of this entire question, and an extended consideration of the authorities upon it, has led to the conclusion that this is the true rule: Officers of a corporation, who are also directors, and who, without any agreement, express or implied, with the corporation or its owners, or their representatives, have voluntarily rendered their services, can recover no back pay or compensation therefor; and it is beyond the powers of the board of directors, after such services are rendered, to pay for them out of the funds of the corporation, or to create a debt of the corporation on account of them. But such officers, who have rendered their services under an agreement, either express or implied with the corporation, its owners or representatives, that they shall receive reasonable, but indefinite compensation therefor, may recover as much as their services are worth; and it is not beyond the powers of the board of directors to fix and pay reasonable salaries to them *after they have discharged the duties of their offices.*" '
(Italics ours.)

From *Waters v. American Finance Co.* (Md.), 62 Atl. 357 (Br. p. 68):

"But, although we so find as to the alleged contract set out in the account, we are of opinion that there was error in granting this prayer. There was evidence tending to show that the appellant did sell at least 2,500 of the 3,500 shares of stock to Mr. and Mrs. Center—included in the subscription we

have spoken of. It is further shown that the appellee actually had in hand at least $5,000 of the money of the Giroux Company for a stock sold Mrs. Center, and in a statement written on the back of a check of the American Finance Company, dated April 11, 1904, payable to the Giroux Company, it credited itself with the commissions on the sale of the 3,500 shares of stock. If then the appellant did sell part of that stock, as he claims he did, and the appellee has in hand the fruits of the labors of the appellant, it would seem to be just that he should receive such compensation as may be found to be reasonable for any services thus rendered by him outside of his duties as vice president or director. There is nothing in the record to show that the sale of the stock was a part of his duties in either of those capacities, and it certainly could not have been required of him to go to Boston for such purpose."

Fitzgerald & Mallory Const. Co. v. Fitzgerald, 137 U. S. 100, 34 L. Ed. 608 (Br. p. 69):

"The character of all these services placed them outside of official duties proper.

"The general rule is well stated by *Mr. Justice Morton* (since chief justice of Massachusetts) in *Pew v. First Nat. Bank,* 130 Mass. 391, 395; 'A bank or other corporation may be bound by an implied contract in the same manner as an individual may. But, in any case, the mere fact that valuable services are rendered for the benefit of a party does not make him liable upon an implied promise to pay for them. It often happens that persons render services for others which all parties understand to be gratuitous. Thus, directors of banks and of many other corporations usualy receive no compensation. In such cases, however valuable the services may be, the law

does not raise an implied contract to pay by the party who receives the benefit of them. To render such party liable as a debtor under an implied promise, it must be shown, not only that the services were valuable but also that they were rendered under such circumstances as to raise the fair presumption that the parties intended and understood that they were to be paid for; or, at least, that the circumstances were such that a reasonable man in the same situation with the person who receives and is benefited by them would and ought to understand that compensation was to be paid for them.' Tested by this rule, we think that the court fairly left it to the jury to determine whether Fitzgerald rendered services of such a character and under such circumstances that he was entitled to claim compensation therefor."

Gumaer v. Cripple Creek Tunnel, etc. Co. (Colo.), 90 Pac. 81 (Br. p. 69):

"The second contention of appellant is that the $8,000 note was made without consideration, and was practically a gift to defendant Wallace. Appellant contends that the evidence as to the alleged services for which the $8,000 was allowed falls far short of showing that they were outside of the line of his duty as an officer and director of the company. There is no evidence that the president or any of the members of the board of directors was bound to perform any duties in addition to those usually performed by like officers in similar corporations. Without attempting to enumerate the ordinary duties of such officers, it is sufficient to say that the services performed by defendant Wallace were largely in excess of those which he was bound to perform as an officer of the corporation. It appears from

the testimony that Wallace spent a great deal of time and rendered valuable services to the company; that he saved the company's entire property from being sold under execution and under decrees to satisfy miners' and mechanics' liens; that he undertook the placing of the stock of the company; that he assumed the entire supervision of the tunnel work and disbursement of the funds, the employment of men, and the making of contracts. His services differed from the other officers of the company, in that he devoted almost his entire time for a portion of each year to the financing and management of the corporation affairs. He was put to much expense in railroad and traveling expense. He gave of his stock to others and secured their assistance, including the 3,750 shares presented to plaintiff. Obviously, therefore, under the testimony, the services which the plaintiff performed were not those of a director or president, but outside thereof and similar to those of a general manager. Corinne Mill, Canal & Stock Co. v. Toponce, 152 U. S. 405, 14 Sup. Ct. 632, 38 L. Ed. 493. In Ruby Chief M. & M. Co. v. Prentice, 25 Colo. 4, 52 Pac. 210, it was said: 'Under the latter and better reasoned cases, for such services (that is, services performed by a director clearly outside of his duties as such director and in the nature of the duties of a general manager or superintendent) a recovery may be had either under an express or implied contract. * * * In Brown v. Silver Mines, 17 Colo. 421, 30 Pac. 66, 16 L. R. A. 426, there was no occasion to announce the rule that should govern in this jurisdiction, nor, as a matter of fact, was there any such ruling. In the absence of a controlling precedent of our own, it is a salutary general rule to follow the decision of the Supreme

Court of the United States. For services clearly outside the director's duties, as a director, we think there may be a recovery; as upon *quantum meruit,* under, and in accordance with, what, in Brown v. Silver Mines, *supra,* is denominated the "more liberal rule." ' The testimony clearly showing that the duties performed by Wallace were in addition to those which he was required to perform as the president or a director of the corporation, he is entitled to compensation therefor, and the court erred in enjoining the collection of so much of the judgment as was based upon the $8,000 note."

Montana Tonopah Mining Co. v. Dunlap (C. C. A. 9th), 196 Fed. 612 (Br. p. 69):

"Notwithstanding the fact that there was no definite and valid exception to the charge of the court, we have nevertheless examined the charge, and find that it contains a full and fair statement of the law applicable to the case as presented by the evidence. It is in accordance with the decisions of the Supreme Court upon the subject, and with the great weight of authority in this country. In the case of Fitzgerald Construction Company v. Fitzgerald, 137 U. S. 98, 111, 11 Sup. Ct. 36, 41 (34 L. Ed. 608), the court approved the following statement of the general rule:

" 'A bank or other corporation may be bound by an implied contract in the same manner as an individual may. But in any case, the mere fact that valuable services are rendered for the benefit of a party does not make him liable upon an implied promise to pay for them. It often happens that persons render services for others which all parties understand to be gratuitous. Thus directors of

banks and of many other corporations usually receive no compensation. In such cases, however valuable the services may be, the law does not raise an implied contract to pay by the party who receives the benefit of them. To render such a party liable as a debtor under an implied promise, it must be shown, not only that the services were valuable, but also that they were rendered under such circumstances as to raise the fair presumption that the parties intended and understood that they were to be paid for; or, at least, that the circumstances were such that a reasonable man, in the same situation with the person who receives and is benefited by them, would and ought to understand that compensation was to be paid for them.'

"In the case of National Loan & Investment Company v. Rockland Company, 94 Fed. 335, 338, 36 C. C. A. 370, 373, the Court of Appeals for the Eighth Circuit had before it the fundamental question here involved, and summed up its conclusions in respect to it as follows:

" 'A thoughtful and deliberate consideration of this entire question, and an extended consideration of the authorities upon it, has led to the conclusion that this is the true rule: Officers of a corporation, who are also directors, and who, without any agreement, express or implied, with the corporation or its owners, or their representatives, have voluntarily rendered their services, can recover no back pay or compensation therefor; and it is beyond the powers of the board of directors, after such services are rendered, to pay for them out of the funds of the cor poration, or to create a debt of the corporation on account of them. Jones v. Morrison, 31 Minn. 140, 147, 16 N. W. 854; Blue v. Bank, 145 Ind. 518,

522, 43 N. E. 655; Doe v. Transportation Co. (C. C.) 78 Fed. 62, 67; Association v. Stonemetz, 29 Pa. 534; Railroad Co. v. Ketchum, 27 Conn. 170; Road Co. v. Branegan, 40 Ind. 361, 364. But such officers who have rendered their services under an agreement, either express or implied, with the corporation, its owners or representatives, that they shall receive reasonable, but indefinite, compensation therefor, may recover as much as their services are worth; and it is not beyond the powers of the board of directors to fix and pay reasonable salaries to them after they have discharged the duties of their offices. Missouri River Co. v. Richards, 8 Kan. 101; Rogers v. Railway Co., 22 Minn. 25, 27; Railroad Co. v. Tiernan, 37 Kan. 606, 15 Pac. 544, 553; Stewart v. Railroad Co. (C. C.), 41 Fed. 736, 739; Rosborough v. Canal Co., 22 Cal. 557, 562.'

"See, also, Corinne Mill, Canal & Stock Co. v. Topence, 152 U. S. 405, 14 Sup. Ct. 632, 38 L. Ed. 493; Clark & Marshall on Private Corporations, §671c, p. 2053; 2 Cook on Corporations (6th Ed.), §657, p. 1929 *et seq.*, and the numerous cases there cited."

Denman v. Richardson (C. C. A. 9th), 292 Fed. 19 (Br. p. 69):

"We find no error in the refusal to instruct the jury that the defendant while acting as trustee could not recover pay for past services, in the absence of some express provision therefor by statute, charter, or by-laws, or some agreement to that effect made and entered into before the services were rendered. The corporation was dissolved after having conducted its business for a period of about 19 years. It had offices at Tacoma, Wash., and branches in Alaska,

British Columbia, and Scotland. It owned ranches in Alberta. It had 5,000 head of cattle. It raised large crops of wheat. It owned and operated steamers and cold storage plants. *The president was not by the by-laws made the manager of the corporation.* The liquidation of the assets was a matter entirely distinct from the management of the corporation. There was evidence that the services rendered by the defendant were of a value much greater than the sum which was paid him, that the liquidation was very ably managed, that it was all done under the immediate direction of the defendant, and that it was wholly outside of the scope of his duties as fixed by the by-laws. In Bloom v. Bloom Codfish Co., 71 Wash. 41, 127 Pac. 596, the Supreme Court of Washington affirmed the general rule that where a president of a corporation renders services as a general manager with the consent of the other officers, he may recover on an implied contract for such services without any express contract therefor. In Fitzgerald Const. Co. v. Fitzgerald, 137 U. S. 98, 11 Sup. Ct. 36, 34 L. Ed. 608, the court held that while an officer of a corporation may recover compensation for performing the usual and ordinary duties of his office, only when there is an express agreement therefor, yet he may be entitled to compensation under an implied contract where he has performed services clearly outside his ordinary duties under circumstances which indicate that it was understood by the other officers of the corporation and by himself that his services were to be paid for. This court made application of the rule in Montana Tonopah Mining Co. v. Dunlap, 196 Fed. 612, 116 C. C. A. 286, holding that an officer or director of a corporation may recover reasonable compensation for services rendered for the corporation outside the

scope of his official duties, if the services were rendered under such circumstances as to raise the fair presumption that the parties intended and understood that they were to be paid for it. Among other cases so holding are National Loan & Investment Co. v. Rockland Co., 94 Fed. 335, 36 C. C. A. 370, and see 7 R. C. L. 465; 14a C. J. 137." (Italics ours.)

Zellerbach v. Allenberg, 99 Cal. 57, 33 Pac. 786 (Br. p. 69):

"It appears from the statement that it was shown at the trial 'that Allenberg had rendered various services other than those required of him as secretary, and had received the sum of $2,400 therefor,' and that the payment of this sum was authorized by a resolution passed by the board of directors of the company. The only evidence brought up in the record to show that the allowance and payment were improper is that of Mr. Zellerbach, in which he stated 'that in 1879 the trustees of the Altoona Quicksilver Mining Company voted Allenberg a compensation of $2,400 for services outside of his secretary's work, against which he, Zellerbach, protested as strongly as he could.'

"It was proper, if Allenberg performed extra services, that he be paid a reasonable and just compensation therefor, and that he did perform such services and received only a reasonable compensation for them *must be assumed in view of the action of the board.* Of course, he could not, as a member of the board, himself take part in passing the resolution to pay him the money, *and it does not appear that he or even E. L. Goldstein did take any part in passing it. There were five directors, and in the*

absence of anything to the contrary, it will be presumed that the resolution was authorized and was properly passed." (Italics ours.)

Appropriate excerpts from *Bassett v. Fairchild,* 132 Cal. 637, 52 L. R. A. 611, 64 Pac. 1082 (Br. p. 69) on the same point:

"Immediately after the organization of the corporation, and in September, 1891, Fairchild was duly elected vice-president and general manager, and remained such during the time mentioned in the complaint. He immediately commenced to perform his duties as general manager, which duties were numerout and onerous, and occupied almost his entire time. The various kinds of work which he did as manager fully appear in the evidence, and need not be here given in detail; it is sufficient to say that his work included direction and supervision of the mining operations in the various leased mines; the supplies required; contracting for hauling rock from mines to cars; purchasing sacks for the rock; attending to shipping-receipts and collecting moneys; securing transportation facilities; chartering vessels for shipping rock to points on the northern Pacific coast; seeing that cars which came to San Francisco were properly loaded and delivered in proper shape to purchasers; looking after office management, and attending to all 'business of the corporation which came along from day to day.' Before his employment he had visited points as far north as Vancouver, British Columbia, in the interest of the use and sale of bituminous rock, and had become acquainted with public officials and others having control of street-paving, and was thus enabled to procure contracts with them for sale of the rock of the corporation. There is no doubt that his services were highly valuable, and

there is no doubt that they were of such a character as to preclude any reasonable supposition that they were to be gratuitous. *But there was no resolution of the board of directors and no express contract determining what compensation he should have for his services as manager, prior to November 9, 1892; and for this reason it is contended by respondents that he cannot legally have any compensation prior to that date.* Fairchild expected to receive compensation for his work as manager, the amount to depend somewhat upon the volume of business that would be developed and the testimony of Walrath, president, and Perine, treasurer of the corporation, shows that it was not expected by them or the other directors that he was to work gratuitously; Moreover, his work as manager was done with the knowledge of the directors, but there was no formal action taken on the subject until November 9, 1892." (Italics ours.)

And further on the lack of necessity of a formal allowance of compensation by the board of directors, pages 642-645:

"The by-laws provide that 'the compensation and terms of office of all officers of the corporation (other than directors) shall be fixed and determined by the board of directors.' *This language does not, on its face, mean that the compensation must be expressly and definitely agreed upon and settled before performance of the services;* but respondents contend that under the general law established by judicial decisions there can be no lawful allowance to an officer of a corporation for services, no matter what their character and value, where the amount of the compensation had not been fixed prior to the rendition of the

services. Many authorities on this subject have been cited on both sides, and they are to some extent conflicting. Most of those cited by respondents merely declare the rule that a 'director' *as such,* without some previous understanding, is not entitled to pay for services which are within the ordinary duties to be expected of him as director, although some of them, no doubt, apply the rule to other officers or agents who are also directors; but as to the last proposition the weight of authority and reason is the other way. (Italics ours.)

"As a general rule, when one person performs valuable services for another, whether the other be a corporation or a natural person, the law raises an implied promise to pay a reasonable compensation for the services, unless they are performed under circumstances which show an understanding that they were to be gratuitous. It frequently happens that one natural person performs valuable services for another natural person for which the former cannot recover, because circumstances show that they were rendered without any expectation of compensation. Now, it has been held that directors of corporations cannot, without previous express contract, receive compensation for such ordinary services as are usually rendered by directors without pay, for the common understanding, as declared by judicial decisions, is, that such services are presumed to be rendered gratuitously. But that presumption does not apply to those onerous services performed by officers and agents of a corporation, though they be also directors, for which compensation is usually demanded and allowed, and which could not reasonably be expected to be performed for nothing. The correct rule is stated by the United States Supreme Court in *Fitzgerald etc. Const.*

Co. v. Fitzgerald, 137 U. S. 98. In that case, Fitzgerald, who was a director of a corporation and its treasurer, acted as superintendent and general manager, and, as such, did valuable work 'not at all pertaining to his office as director,' and the question was, whether he was entitled to compensation for such work done before any compensation was fixed. The opinion of the court states that the trial court 'instructed the jury that, "if Fitzgerald, the plaintiff, acted as superintendent, treasurer, or general manager of said company, and transacted the usual business that devolves upon such officer of such a concern as that, with the knowledge and consent of the defendant" (during the time before compensation was fixed), there would be an implied agreement on the part of the defendant to pay what the services are reasonably worth, and afterwards repeated this instruction more in detail, confining it to services as manager.' The verdict was for Fitzgerald, and the judgment was affirmed. The court said: 'The general rule is well stated by Mr. Justice Morton (since chief justice of Massachusetts) in *Pew v. First Nat. Bank etc.,* 130 Mass. 391, 395: "A bank or other corporation may be bound by an implied contract in the same manner as an indiidual may. But, in any case, the mere fact that valuable services are rendered for the benefit of the party does not make him liable upon an implied promise to pay for them. It often happens that persons render services for others which all parties understand to be gratuitous. Thus directors of banks and of many other corporations usually receive no compensation. In such cases, however valuable the services may be, the law does not raise an implied contract to pay by the party who receives the benefit of them. To render such party liable as a debtor under an implied promise, it must

be shown not only that the services were valuable, but also that they were rendered under such circumstances as to raise the fair presumption that the parties intended and understood that they were to be paid for; or, at least, that the circumstances were such that a reasonable man, in the same situation with the party who receives and is benefited by them, *would and ought to understand that compensation was to be paid for them.*" Tested by this rule, we think that the court fairly left it to the jury to determine whether Fizgerald rendered services of such a character and under such circumstances that he was entitled to claim compensation therefor. *It could not properly have been held, as matter of law, that he was not so entitled.*' (Italics the Court's.)

"*Rogers v. Hastings etc. Ry. Co.,* 22 Minn. 25, is a case directly in point. It is stronger in support of the proposition above stated than the case at bar, because the charter of the corporation in that case provided that the board of directors should appoint the officers 'and fix their compensation for the services *to be rendered.*' Rogers was a director, and was appointed secretary of the corporation, and also acted as its land commissioner and attorney, and sued for the value of services rendered in such capacities. There had been no compensation fixed, nor any contract made, before the services were rendered; and it was contended there, as here, that no compensation could be recovered for past services. But it was held otherwise. The court said, among other things, as follows: 'The evidence showed that the plaintiff, while acting as land commissioner, was a member of the board of directors. If his services as land commissioner had been performed by him simply *as a director,* it might be that he could not recover for the same, since, in the absence of a special agreement for

compensation, he would, according to many authorities, be presumed to have acted gratuitously. But the duties and labors of a land commissioner of a land-grant railroad company do not necessarily nor presumptively pertain to a director as such. Indeed, it would be unreasonable to suppose that duties so onerous would be undertaken by one acting simply as a director without pay. For such extraordinary services, outside of and beyond his duties as director, a party may certainly recover, notwithstanding his directorship, for the reason that, even if he performs the duties of director gratuitously, these services are not a part of those duties.' (Citing cases.)" (Italics the Court's.)

Appropriate excerpts from *King v. Grass Valley Gold Mines Co.*, 205 Cal. 698, 272 Pac. 290 (Br. p. 69):

"In short, we see no reason here for withholding application of the rule announced in the case of *Bassett v. Fairchild*, 132 Cal. 637 (52 L. R. A. 611, 64 Pac. 1082), to the effect that the presumption that certain corporate officers render their services gratuitously in the absence of previous express contract, does not apply to onerous services, which could not reasonably be expected to be performed for nothing, although no compensation therefor is previously fixed; and in such cases there is an implied agreement to pay what the services are reasonably worth."

Excerpt from *San Leandro Canning Co. Inc. v. Perillo*, 84 Cal. App. 635 (Br. p. 69):

"As to the two director-defendants, it is alleged that neither of them had a prior contract or agreement with said corporation whereby they, or either

of them, was to be paid a commission for making sales of the corporate stock. As we understand the argument of the appellant it is to the effect that the claims for compensation of the two director-defendants were, therefore, *ultra vires* the corporation and could not legally be paid. If this were an action by said directors to recover compensation for the value of their services so rendered, it will be conceded at once that a prior authorization would be of importance. But that rule is not without limitation. In *Bassett v. Fairchild,* 132 Cal. 637, 643 (52 L. R. A. 611, 64 Pac. 1082), the court said: 'Now, it has been held that directors of corporations cannot, without previous express contract, receive compensation for such ordinary services as are usually rendered by directors without pay, for the common understanding, as declared by judicial decisions is, that such services are presumed to be rendered gratuitously. But that presumption does not apply to those onerous services performed by officers and agents of a corporation, though they be also directors, for which compensation is usually demanded and allowed, and which could not reasonably be expected to be performed for nothing.' (See, also, *Hughes v. Pacific Wharf etc. Co.,* 188 Cal. 210, 216 (205 Pac. 105).) But we are running afield. *This is not an action by a director to recover compensation. The complaint alleges that the directors have already been paid. This is an action to recover back those payments.* Counsel do not cite any authorities, and we know of none, to the effect that, in the absence of allegations of fraud, the mere averment that without a prior authorization the payment to a director for services admittedly rendered would be either a void or a voidable transaction." (Italics ours.)

QUOTATIONS FROM CASES CITED BY APPELLANT AT PAGE 40 OF ITS BRIEF.

Jones v. Foster (C. C. A. 4th), 70 Fed. (2d) 200 (Br. p. 70):

> "In instructing the jury to disallow this claim the district judge acted on the view that the services performed were clearly not outside the scope of the duties pertaining to the defendant's office as president of the corporation in accordance with the By-Laws, especially when considered in the light of the original agreement or understanding between the parties and bearing in mind the defendant's personal interest as majority stockholder of the corporation and relation of creditor by virtue of the substantial loans to the corporation for working capital. In our opinion the view so taken is reasonable and sound. In the absence of an express agreement by the corporation to pay for services *within the scope of the officer's duties* there could be no valid claim for compensation. Baltimore Co. v. Dinning, 141 Md. 318, 321, 118 A. 801." (Italics ours.)

From syllabus in *Pindell v. Conlon Corp.* (Ill.), 24 N. E. (2d) 882 (Br. p. 71):

> "A director was not entitled to compensation for allegedly obtaining a manufacturing contract for corporation, where alleged oral agreement with president of corporation provided for the securing of a purchaser for corporation and not a manufacturing contract, and director, in absence of a by-law or resolution of board of directors, was not entitled to compensation for services rendered *within the scope of his duties as a director.*" (Italics ours.)

From syllabus in *Larkin v. Enright,* 37 N. E. (2d) 905 (Br. p. 71):

"*Corporations*

"In suit to restrain defendant from voting two shares of stock standing in his name on books of corporation, evidence disclosed that plaintiff delivered stock to defendant to hold for a limited use and to be returned by request, and that plaintiff was the legal owner of the two shares involved.

"*Corporations*

"Where defendant was director and secretary of corporation and an employee receiving $75 weekly when he obtained reduction of corporation's mortgage indebtedness and an extension of the mortgage, he was not entitled to extra compensation in the absence of a by-law or resolution authorizing payment thereof.

"*Corporations*

"Contention that person who was president of corporation promised employee, who was a director and secretary, 'at some later date to make it all right with him' for his services in obtaining reduction and extension of corporation's mortgage, was too vague and uncertain to form basis of a contractual obligation.

"*Corporations*

"Where president of corporation agreed that one who was employee and stockholder should hold two shares of stock belonging to president for limited use and return it upon request, failure to return stock justified court in restraining holder from using such stock to gain control of corporate affairs."

In re Dr. Voorhees Awning Hood Co. (D. C. Pa.), 187 Fed. 611 (Br. p. 71):

> "The other matters were correctly disposed of except one, and require no extended consideration. The claimant, being president of the company, had no right to a commission on sales either of stock or material, except as there was a distinct agreement to that effect, which has not been shown. Althouse v. Cobaugh Colliery Co., 227 Pa. 580, 76 Atl. 316. It affords no basis for such a claim that they were allowed to others. Nor is it of any consequence that $138 was actually paid him by the company on this account. Just how this came about does not appear. The directors may have felt that he ought to be remunerated to that extent for his services in this connection without thereby establishing his rights as a legal claim to the remaining $62 contended for."

EXCERPTS FROM CASES CITED ON THE QUESTION OF THE PROPRIETY INTEREST OF THE INDIVIDUAL DEFENDANTS IN THEIR INVENTIONS AND DEVICES, AS WELL AS SHOP RIGHTS THEREIN, IN THE ABSENCE OF COMPENSATION THEREFOR AND ASSIGNMENTS THEREOF.

United States v. Dubilier Corp., 289 U. S. 178, 77 L. Ed. 1114 (Br. p. 72):

> "A patent is property and title to it can pass only by assignment. If not yet issued an agreement to assign when issued, if valid as a contract, will be specifically enforced. The respective rights and obligations of employer and employee, touching an invention conceived by the latter, spring from the contract of employment.
>
> "One employed to make an invention, who succeeds, during his term of service in accomplishing that

task, is bound to assign to his employer any patent obtained. The reason is that he has only produced that which he was employed to invent. His invention is the precise subject of the contract of employment. A term of the agreement necessarily is that what he is paid to produce belongs to his paymaster. Standard Parts Co. v. Peck, 264 U. S. 52, 68 L. ed. 560, 44 S. Ct. 239, 32 A. L. R. 1033. On the other hand, if the employment be general, albeit it covers a field of labor and effort in the performance of which the employee conceived the invention for which he obtained a patent, the contract is not so broadly construed as to require an assignment of the patent. Hapgood v. Hewitt, 119 U. S. 226, 30 L. ed. 369, 7 S. Ct. 193; Dalzell v. Dueber Watch Case Mfg. Co., 149 U. S. 315, 37 L. ed. 749, 13 S. Ct. 886. In the latter case it was said:

" 'But a manufacturing corporation, which has employed a skilled workman, for a stated compensation, to take charge of its works, and to devote his time and services to devising and making improvements in articles there manufactured, is not entitled to a conveyance of patents obtained for inventions made by him while so employed, in the absence of express agreement to that effect.'

"The reluctance of courts to imply or infer an agreement by the employee to assign his patent is due to a recognition of the peculiar nature of the act of invention, which consists neither in finding out the laws of nature, nor in fruitful research as to the operation of natural laws, but in discovering how those laws may be utilized or applied for some beneficial purpose, by a process, a device or a machine. It is the result of an inventive act, the birth of an idea and its reduction to practice; the product of

original thought; a concept demonstrated to be true by practical application or embodiment in tangible form. Clark Thread Co. v. Williamantic Linen Co., 140 U. S. 481, 489, 35 L. ed. 521, 525, 11 S. Ct. 846; T. H. Symington Co. v. National Castings Co., 250 U. S. 383, 386, 63 L. ed. 1045, 1049, 39 S. Ct. 542; Pyrene Mfg. Co. v. Boyce (C. C. A. 3d) 292 Fed. 480, 481.

"Though the mental concept is embodied or realized in a mechanism or a physical or chemical aggregate, the embodiment is not the invention and is not the subject of a patent. This distinction between the idea and its application in practice is the basis of the rule that employment merely to design or to construct or to devise methods of manufacture is not the same as employment to invent. Recognition of the nature of the act of invention also defines the limits of the so-called shop right, which shortly stated, is that where a servant, during his hours of employment, working with his master's materials and appliances, conceives and perfects an invention for which he obtains a patent, he must accord his master a non-exclusive right to practice the invention. McClurg v. Kingsland, 1 How. 202, 11 L. ed. 102; Solomons v. United States, 137 U. S. 342, 34 L. ed. 667, 11 S. Ct. 88; Lane & Co. v. Locke, 150 U. S. 193, 37 L. ed. 1049, 14 S. Ct. 78. This is an application of equitable principles. Since the servant uses his master's time, facilities and materials to attain a contract result, the latter is in equity entitled to use that which embodies his own property and to duplicate it as often as he may find occasion to employ similar appliances in his business. But the employer in such a case has no equity to demand a conveyance of the invention, which is the original conception of the em-

ployee alone, in which the employer had no part. This remains the property of him who conceived it, together with the right conferred by the patent, to exclude all others than the employer from the accruing benefits. These principles are settled as respects private employment."

On the same point from *Deane v. Hodge* (Minn.), 27 N. W. 917 (Br. p. 72):

"Where the evidence fails to disclose an express agreement or understanding, the law may imply a contract from the circumstances or the acts of the parties; and where there is nothing from which a contrary intention or understanding is to be inferred, it is a just and reasonable presumption that he who has received the benefit of the services or property of another impliedly undertakes to make compensation therefor. 'Implied contracts are such as reason and justice dictate, and which, therefore, the law presumes that every man has contracted to perform.' 3 Bl. Comm. *158; 2 Kent, Comm. *450; Bouv. Law Dict. 'Obligations, Implied;' 2 Greenl. Ev. §108. A patent is a mere monopoly or exclusive right to an invention, not existing at the common law, but by special grant from the government. The defendant therefore contends that, unless there is an express contract defining the terms of use by a licensee, the patentee is confined to the remedy provided by the patent law for an infringement, by an action on the case for damages, and that there can be no such thing as an implied license for compensation.

"There is very little authority on the subject, as the question of implied license has usually arisen in actions for infringement, and as such is for a

tortious use or piracy, and the existence of a license, express or implied, is always a sufficient defense. But an action upon a contract, express or implied, for compensation for the use of a patented invention, or for license fees, is not one arising under the patent laws; and, notwithstanding the nature of the subject, common-law principles are applicable, as in other cases. Thus, in *McClurg v. Kingsland, supra,* the court held that, if the facts were as testified, 'they would justify the presumption of a license or special privilege or grant to the defendants to use the invention, and show such a consideration as would support an express license or grant, or *call for a presumption of one, to meet the justice of the case,* by exempting them from liability, having equal effect with a license, and giving the defendants *a right to the continued* use of the invention.' Here is recognized the principle that, from the circumstances and to meet the justice of the case, a license or grant for a continued use of the invention would be implied. The right to use and profit by a patented invention may, then, be the subject of contract; and if the evidence of an express contract is wanting, it may be implied, as in other cases, and for the same reasons; and if *assumpsit* will lie upon express contract to recover reasonable license fees or compensation, it may also be maintained upon implied contract, though, from the nature of the subject, and the circumstances of any particular case, the question may be involved and difficult of solution. See Walk. Pat., §312; *DeWitt v. Elmira Manuf'g Co.*, 66 N. Y. 461. In *McKeever v. U. S.*, 14 Ct. Cl. 396, it was held that where the patentee had allowed the defendant to proceed in the manufacture and use of a patented invention or article 'without the formality of an express license, or the precaution

of an express consideration, the omission did not change the character of the transaction, for the law supplies, by implication, a price in giving what the license was reasonably worth.' The case was well considered, and was afterwards affirmed by the supreme court of the United States. Walk. Pat. §391.

"Recurring again to the question of the relationship of the plaintiff to the defendant as president or director at the time, as affecting his cause of action, it was held in *Rogers v. Railroad,* 22 Minn. 25, that a defendant corporation, or which the plaintiff was a director, might be held liable upon an implied *assumpsit* to pay the reasonable value of services rendered for defendant outside of his duties as director. He could not, as director, aid by his vote in fixing the amount of such compensation, for in that case there would be a conflict of interests inconsistent with his official duty. *Jones v. Morrison,* 31 Min. 148; S. C. 16 N. W. Rep. 854. But the rule is not, as we understand it, to be carried so far as to prevent the corporation from availing itself of the services or property of an officer of the company, 'if necessary for its convenience or profits, as in the case of other persons, under circumstances implying a contract to pay a reasonable compensation therefor.' *Rider v. Rubber Co.,* 5 Bosw. 97. All such dealings are, of course, looked upon with jealousy by the courts, and the fact of such official relationship, and the interest of the officer in the affairs and property of the corporation, would figure prominently in determining the question of fact whether or not a contract for a compensation is to be implied. *Gardner v. Butler,* 30 N. J. Eq. 703.

"Upon the directors was imposed the duty and authority, which was exercised by them, of determining the character and number of the machines

to be manufactured. The improvement was appropriated and used by them, or under their direction, on behalf of the company; and the continued acquiescence of the corporation for several years sufficiently indicate its approval. *Rider v. Rubber Co.*, 5 Bosw. 96." (Italics the Court's.)

Heywood-Wakefield Co. v. Small (C. C. A. 1st), 87 Fed. (2d) 716 (Br. p. 72):

"The defendant has a large factory in which it manufactures, *inter alia*, car seats for trolley cars and railroad coaches. It first employed the plaintiff in the fall of 1927 as a draftsman. This employment continued until March, 1928, when Small was promoted and made a 'checker.' It was while employed as a checker in July, August, and September, 1928, that Small invented the car seat base for which the patent in suit was issued.

"The defendant contends that the plaintiff was employed to invent improvements in its line of goods and that the results of his efforts at invention belong to his employer. Houghton v. United States (C. C. A.) 23 F. (2d) 386, 390; United States v. Dubilier Condenser Corp., 289 U. S. 178, 53 S. Ct. 554, 77 L. Ed. 1114, 85 A. L. R. 1488. The plaintiff says that his employment was not of that character. There was some conflict of testimony as to what duties were involved in plaintiff's work as 'checker.' The defendant's contention was that if the plaintiff 'saw, as he checked through the work, that improvements could be made on it, * * * he could offer these suggestions and have changes made in the drawings' that such duties 'went with the position of checking.' The plaintiff testified that his duties were 'to check every part of the car seat, and all parts of the car seat,—reed furniture shop, machine shop,

wood shop, upholstery shop, cutting room, and paint shop. My work was entirely on car seats. * * * It was my job to see that the goods were made according to the orders.' The plaintiff's immediate superior, a Mr. Eichel, testified that: 'The duties of checker were to look over the products of manufacture whenever it was requested from the shop, the foreman or the superintendent.' We generally went down, looked them over and passed on them. And then before the article went through to another department that was going to use it, they would request a check on it. The checker would change the orders, would check the drawings in the drafting room and check the work in the shop from those drawings.

"Eichel further testified that he did not recall ever having given the plaintiff definite orders to design a rotating car seat base; and no such instructions appear to have been given to the plaintiff by anybody else. Nor does it appear that the plaintiff was ever assigned to the work of inventing improvements on the company's products.

"In finding that 'originating new developments was not part of the plaintiff's duties in this capacity (as checker)' it certainly cannot be said that the District Judge was clearly in error. It follows that the defendant was not entitled to an assignment of the patent."

On the question of "shop rights" the Court says:

"On the question of whether the defendant was entitled to a 'shop right' either upon the basis of a contract on the ground that the work of invention was on the defendant's time and at its expense, or on the ground of estoppel, that he saw his inven-

tion being used by the defendant without protest on his part, none of the cases cited supports the defendant's contention.

"The cases of McClurg v. Kingsland, 1 How. 202, 11 L. Ed. 102; Solomons v. United States, 137 U. S. 342, 346, 11 S. Ct. 88, 34 L. Ed. 667; Lane & Bodley Co. v. Locke, 150 U. S. 193, 14 S. Ct. 78, 37 L. Ed. 1049; Keyes v. Eureka Mining Co., 158 U. S. 150, 15 S. Ct. 772, 39 L. Ed. 929; Gill v. United States, 160 U. S. 426, 16 S. Ct. 322, 40 L. Ed. 480, all differ widely from the facts in this case. In these cases either the plaintiff made the invention on his employer's time and at his employer's expense and it was a part of his duty to improve the methods used by his employer, or he stood by for a long period and permitted his employer to use his invention without protest before making any claim.

"Nor do we think the case of John M. Burton v. Burton Stock-Car Co., 171 Mass. 437, 50 N. E. 1029, has any bearing on the issues in this case. In that case there was an assignment of an invention with the stipulation that the plaintiff reserved the right to royalties in the future and was assured by the defendant that that would be adjusted later. The court said, at page 440 of 171 Mass. 50 N. E. 1029, 1030:

" 'There was no evidence, so far as appears, that the plaintiff agreed to license the use of his improvements gratuitously and in the absence of such an agreement an implied promise to pay might be inferred from the above facts. Walk. Pat. (2d Ed.) §312.' "

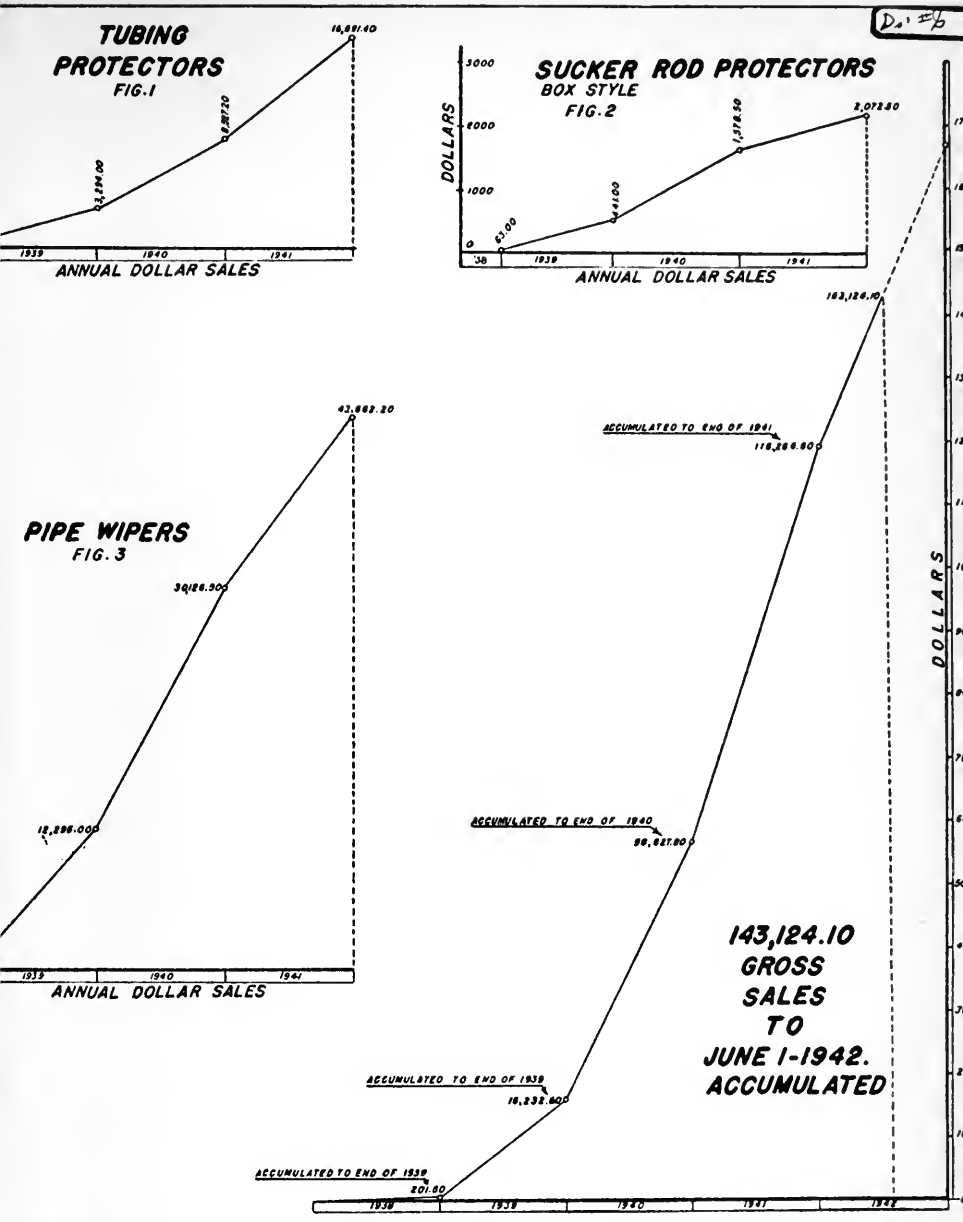
THE FOLLOWING ARE EXCERPTS FROM CASES CITED ON PAGES 76-77 OF THE BRIEF UNDER THE HEADING OF "RATIFICATION".

Middleton v. Arastraville Mining Co., 146 Cal. 219 (Br. p. 76):

> "The suggestion in the appellants' brief that by reason of his interest the plaitniff is disqualified from voting in favor of ratifying the act of the directors is without merit. The stockholders of a corporation do not hold a fiduciary relation to each other by which one is precluded from voting at a stockholders' meeting upon any question in which he has an individual interest adverse to any of the other stockholders." (P. 224.)

Klein v. Independent Brew. Co. (Ill.), 83 N. E. 434 (Br. p. 77):

> "By his conduct subsequent to the meeting of November, 1901, *in participating in the election and re-election of the same officers year after year* and fixing their salaries, including a salary to himself, as director, of $300 per year, he is estopped from now asking an accounting on account of the salaries paid after said year 1901. Brown v. De Young, 167 Ill. 549, 47 N. E. 863; Rosehill Cemetery Co. v. Dempster, 223 Ill. 567, 79 N. E. 276; Cook on Corporations, §646. Furthermore, there is not a word of proof that the services of the officers of the corporation were not worth the salaries paid to them." (P. 442.) (Italics ours.)



GRAPHIC CHARTS INDICATING
THE YEAR BY YEAR INCREASE IN DOLLAR SALES
OF
ROYALTY-FREE INVENTIONS
OF J. C. BALLAGH
OTHER THAN THE INVENTIONS
OF THE LIP PROTECTOR AND HYDRAULIC APPLICATOR

No. 10,473

IN THE

United States Circuit Court of Appeals

For the Ninth Circuit

BYRON JACKSON CO., a corporation,
Appellant,

vs.

PATTERSON-BALLAGH CORPORATION, a corporation, J. C. BALLAGH and D. G. MILLER,
Appellees.

APPELLANT'S REPLY BRIEF.

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No. 10,473

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APPELLANT'S REPLY BRIEF.

Thirty-six pages of appellees' brief are devoted to discussions of the scope of the reviewing power of this Court, the nature of the action (whether at law or in equity), and the burden of proof. These are all interesting subjects and have a bearing on this case. We have discussed them in our opening brief and will again deal with them. We think it more important to first examine, in light of counsel's brief, the uncontradicted proof as appearing in this record.

I. DEFENDANTS' ONLY ATTEMPT TO JUSTIFY THEIR EXCESSIVE SALARIES IS BY RESORT TO THEIR CLAIMED INVENTIONS.

In defendants' brief there is not one claim that defendants' salaries can be justified in any manner other than by resort to inventions. A reading of the brief will not only demonstrate the absence of any claim that the salaries can be otherwise defended but at numerous points this is conceded.

Commencing at the bottom of page 63 of their brief there is the following:

> "They (the defendants) do contend, however, that they are entitled to compensation for their services as president, General Manager and for the development of inventions and devices so far as Miller is concerned, and as secretary-treasurer, Sales Manager and the development of devices and inventions so far as Ballagh is concerned, paid in each case as a unit and not split up into separate categories as in the *Stratis* case, *supra*," etc. (Underscoring ours.)

On page 49 counsel deal with the testimony of Mr. Burrell, the company's attorney, and state as follows:

> "As to the compensation to both Messrs. Ballagh and Miller in so far as the matter of inventions was a factor, it was Mr. Burrell's opinion that the inventions belonged to the inventors in the absence of assignments or licensing agreements. He testifies that they either had been or would be transferred as soon as invented or as soon as patents were applied for (R. 449) and that it was distinctly to the company's ad-

> vantage to compensate Ballagh and Miller for the use of these inventions on a salary basis which was flexible from time to time depending upon the general condition of the business, rather than to definitely obligate the company to pay royalties under licensing agreements (R. 450-451)."

Numerous other illustrations of the foregoing are to be found upon pages 44, 46, 48, 51, 54, 55, 56, 60, 61, 65, 66, and 67 of the brief.[1]

It is not surprising that counsel are forced to rely upon inventions. For the fiscal year 1940 the defendants took from the corporation over $48,000 in salaries. For the fiscal year 1941 defendants took from the corporation over $53,000 in salaries. As pointed out in our opening brief, for the year 1940 defendants

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[1]Counsel, upon pages 61 and 62 of their brief, discuss *Stratis v. Anderson*, 254 Mass. 536, 150 N. E. 832. Their claim that this case is not in point must be due to a misunderstanding. The *Stratis* case held that when an employee of a corporation is compensated in separate amounts for his services as treasurer, for his services as general manager, and for his services as clerk, his excessive compensation in one capacity cannot be justified by his underpayment in another capacity.

The case is absolutely in point. Ballagh and Miller were being compensated as president and general manager and as secretary, treasurer and sales manager. They were not being compensated as inventors. The minutes so demonstrate. Suppose that each of these gentlemen had been paid $1,000.00 a year for his services as president and general manager or secretary, treasurer and sales manager, and suppose that they had also been employed as inventors, for which services they were paid the remaining $48,000.00; their compensation in the latter capacities could not have been justified by the underpayment in the former capacities. This is precisely what the *Stratis* case holds. The present record is even more extreme. They were not even employed as inventors.

We are wondering if Ballagh and Miller had refused to work upon inventions, counsel would maintain they had violated their contracts and should have been discharged.

took unto themselves 70%, and for the year 1941 74%, of the net profits of the corporation. During these years the entire capital and surplus of the corporation was only a little over $200,000. Defendants, during each year, were taking unto themselves an amount equivalent to one-fourth of the entire capital and surplus. The situation is there.

Appellant does not have to resort to the Bunch exhibit. A mere appeal to the general knowledge, common sense, and experience of this Court is sufficient.

Thus defendants are obliged to inject some extraordinary circumstances that do not exist in the normal corporation. They, therefore, rely upon inventions. We again examine the inventions.

II. DEFENDANTS' INVENTIONS CANNOT JUSTIFY EXCESSIVE SALARIES.

1. DEFENDANTS IN ONE BREATH CLAIM THAT THEIR INVENTIONS WERE PROPERTY RIGHTS WHICH, UNTIL CONVEYANCE TO THE CORPORATION, BELONGED TO THEMSELVES. IN THE NEXT BREATH, THEY CLAIM THAT THEIR INVENTIONS CONSTITUTED SERVICES RENDERED TO THE CORPORATION.

This is no better illustrated than by quoting from counsel's brief. On page 72 there is the following:

> "It remains perhaps to establish that the devices and inventions developed by Messrs. Miller and Ballagh originated under circumstances which constituted them their individual property both as to the element of use or so-called 'shop rights'

> and also from the proprietary standpoint and that, in conferring their free use upon the corporation and in assigning their present and future proprietary interest thereto, they were parting with property rights of value. (Underscoring ours.)

Just across on page 73, there is the following:

> "However, the individual defendants devised these inventions with the sole idea and for the sole purpose of improving the company's business and making it the beneficiary in so far as their royalty free use was concerned, and, in addition thereto, conferred the proprietary ownership upon the company. If this does not constitute the rendition of 'services' we do not understand the meaning of that term and, in our opinion, this argument of appellant characterizes and should discredit its case *in toto*." (Underscoring ours.)

Apparently counsel produce a legal hybrid. It has always been our understanding that services are different than property rights, and *vice versa*. We do not understand how an invention can at the same time be both. We are dealing with, not only a hybrid, but an afterthought introduced into this litigation for the first time at the trial in an attempt to justify salaries that can not be justified.

Nevertheless, counsel force us to consider both alternatives; to-wit, the alternative that the inventions constituted property rights belonging to the defendants, and the alternative that the inventions constituted services rendered to the corporation.

(a) The alternative that the inventions constituted property rights.

We have always believed that this is the correct alternative. A patent is property. (*United States v. Dubilier,* 289 U.S. 178.) Commencing at page 35 of our opening brief, we correctly stated that there was no action by the Board of Directors employing the defendants as inventors, without which no reliance in support of salaries could be placed upon inventions. We also showed by the uncontradicted testimony of the defendant Ballagh and of the corporation attorney, Burrell, that the defendants never had any contract to perform such services for the corporation and that when the so-called inventions were perfected they were the property of the defendants, which they could or could not transfer to the corporation, as they saw fit. We, therefore, thought that it was impossible to claim that the inventions were services rendered to the corporation, or that they were services at all. This we submit upon our opening brief.

(b) The alternative that the inventions constituted services rendered to the corporation.[2]

We argued in our opening brief that even if the inventions of the defendants could be considered as services, they are not of sufficient value to support

[2]Counsel, on page 64 of their brief, say that they are wholly at a loss to understand appellant's argument that if services were performed by the defendants such services were performed for themselves and not for the corporation. We concede that counsel have failed to understand our argument. They draw the absurd conclusion that our argument was "all for the purpose of showing that for the compensation paid by the corporation to the inventors, the corporation gained great value which it otherwise would not have received and owned". Not in this respect but in

the amount of the salaries. We will hereafter again consider this.

Counsel claim on page 4 of their brief that Miller was never elected general manager and that Ballagh was never elected sales manager. A statement on page 60 of their brief is entirely inconsistent for there they point out, which was the fact, that on February 15, 1939, at a directors' meeting, Miller was designated general manager and that at a meeting of the Board held on March 18, 1940, it was pointed out that the duties of Ballagh also included that of sales manager. Be this as it may, we are unable to believe that the absence of the employment of these two gentlemen as inventors can be remedied by what may or may not appear in the minutes as to general manager or sales manager.

The Ballagh inventions. Ballagh, in so far as receiving salary was concerned, was the greater of the two offenders. Irrespective of the value of his inventions, there is another conclusive argument that they can not be used to bolster up his salary. The peak of the misappropriation of moneys from the corporation by paying excessive salaries was during the years 1940 and 1941. It is axiomatic that, except by specific contract, salaries during those years can only be for services rendered during those years. The

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another respect our argument may be misleading in that it hypothetically attempts to consider the inventions as services when they were not services at all, but were property rights belonging to the defendants and which were transferred to the corporation just as any chattel or piece of real estate could have been transferred.

inventions upon which Ballagh relies were all perfected either prior to 1939 or during the early part of that year. Before the beginning of 1940, they were well under way.[3] We will consider in turn each invention upon which any emphasis is laid and in the order of the importance which counsel ascribe to them.

The lip protector. There was a sale of this lip protector in 1939. Ballagh so testifies at page 366 of the record. At page 514 he testified that a few of the lip protectors were sold in 1939. Defendants' Exhibit "A",[4] to be found opposite page 10 of this brief, shows that many sales of lip protectors occurred in 1940.

The hydraulic applicator. This applicator was developed before the lip protector, at some time during the years 1936-1938, probably in 1938. At any rate, it had been perfected prior to 1939. At page 455 of the record, the witness Burrell, the corporation's attorney, testified that during the period from 1934 to 1938, he practically lived with the applicator, and that for the last two years of this period he was working on the hydraulic applicator. Ballagh testified that an application for a patent was filed in 1939 (R. 492) and that work had commenced in 1938. There are also other references in the record. (R. 430-431; 460; 462; 531.)

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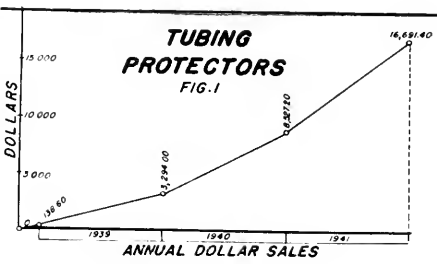
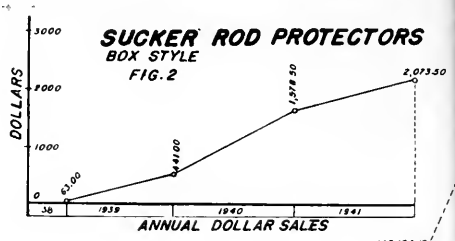
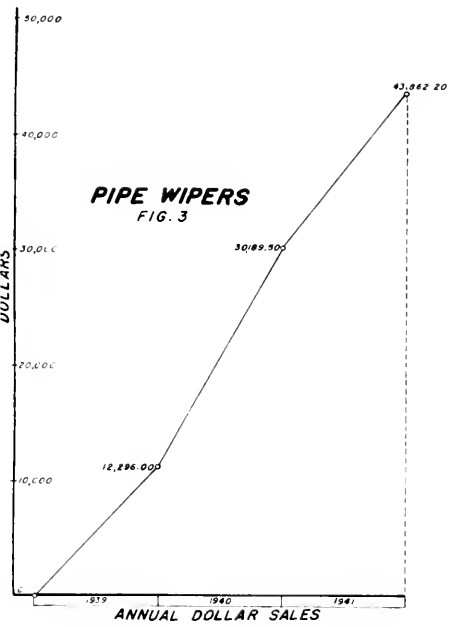
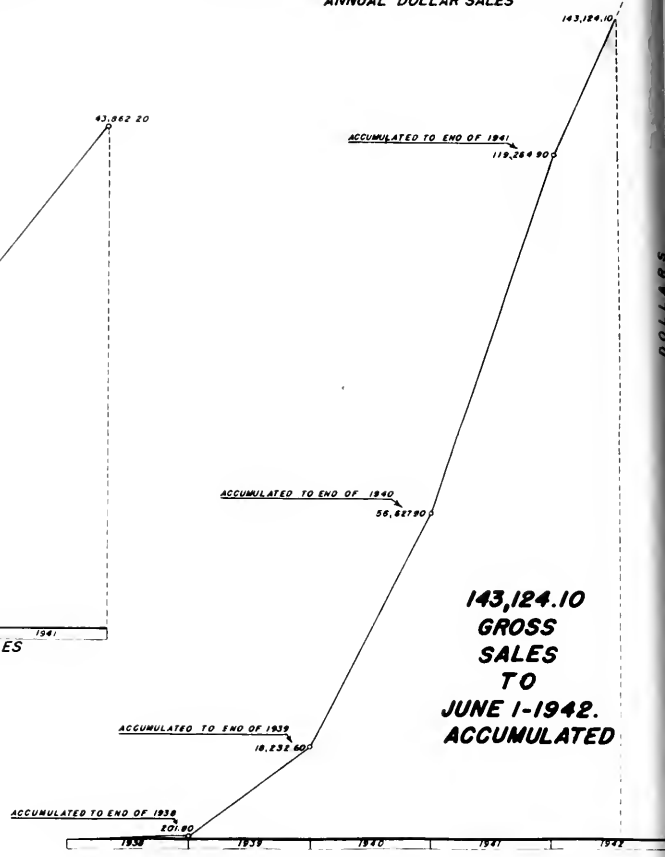
[3]Counsel, at page 5, of their brief, mention references in the minutes to inventive work. The last minutes containing any reference to any such work (we do not know by whom) was December 20, 1938. The conclusion to be drawn therefrom is in exact accord with the above argument.

[4]The only exhibits that plaintiff invokes in this brief are defendants' own exhibits.









GRAPHIC CHARTS INDICATING THE YEAR BY YEAR INCREASE IN DOLLAR SALES OF ROYALTY-FREE INVENTIONS OF J. C. BALLAGH OTHER THAN THE INVENTIONS OF THE LIP PROTECTOR AND HYDRAULIC APPLICATOR

The pipe wiper; the tubing protector; the sucker rod protector. These items are the only other so-called inventions that either Ballagh or his counsel stress.[5] We consider them together because defendants' Exhibit "G" shows conclusively that they all came into being at the latest in 1939 and probably prior thereto. For the Court, we set opposite a photostatic copy of defendants' Exhibit "G" with the comment that as to what we are establishing it is conclusive, but that as to another phase of the case it is misleading. The curves as shown thereon are cumulative, and unless the word "accumulated" as printed thereon is observed, the importance of these three inventions can be many times magnified.

In addition, at page 370 of the record Ballagh testified that he started work in 1938 upon the pipe wiper and that he thought the first sales were made in that year. At page 527 he testified that Exhibit "G" directly portrayed the volume of gross sales of the sucker rod protectors from 1939 to 1941. We have been able to find no data as to tubing protector except Defendants' Exhibit "G", which is therefore uncontradicted. So that the Court may fully understand the relative unimportance of the inventions

[5]Counsel, at page 47 of their brief, mention the Kelly wiper and the plastic tubing protector. These items were trivial. Defendants' Exhibit A shows that in the year 1941 only approximately $1000 worth of Kelly wipers were sold (none appear prior thereto), and Exhibit A does not even mention the plastic tubing protector as a distinct item. Furthermore, the first sales of the plastic tubing protector were made in 1938 (R. 523), and the Kelly wipers, according to Ballagh's own testimony, amounted to nothing more than a larger size of the pipe wiper. As above set forth, the pipe wiper came into being prior to 1939.

listed upon Exhibit "G", we again refer the Court to the photostat of Exhibit "A" inserted opposite.

We have gone further than necessary. At page 48 of counsel's brief the following appears:

> "All of these devices were developed and placed on the market from about the beginning of 1939, * * *"

Thus we find that even if Ballagh could resort to his five claimed inventions they would not bolster up salaries for the years 1940 and 1941. It would be novel if an employee, without any contract with a corporation, could make claim for huge amounts for services in the years 1940 and 1941, when those services were not rendered in those years, but had been rendered during prior years. The minutes do not show any resolution passed during any prior year whereby services rendered in any such year were to be thereafter and in subsequent years compensated. We are wondering, if the defendant Ballagh had left the employ of the corporation upon December 31 of 1939 he would have made claim for compensation for later years, and if so, how many subsequent years he would have mentioned. Was he to have a pension for his life, or a pension during the life of the patents, or what not?

Ballagh testified that it was much better for the corporation to pay large salaries rather than to pay royalties (R. 45; 453-454) and thus attempted to excuse the excess, but this theory was never em-

1938	1939	1940	1941

GROSS ANNUAL SALES DISTRIBUTION BY ITEMS AND INVENTIONS.

1938
312,979.11

LINE GUIDES 26,944.35 — ROYALTY 1108.06

SWIVEL BUMPERS 5766.44
MUD GUNS 3568.50 — 834.82

INSTALL. EQUIP. 14,450.75

CASING PROTECTORS (WITHOUT LIPS) 239,208.06 — 10,870.25

12,813.13 TOTAL

1939
336,527.88

LINE GUIDE 33,322.18 — ROYALTY 730.12

SWIVEL BUMPERS 11,633.33 — 1770.22
MUD GUNS 5,983.31 — 45.99
INSTALL. EQUIP. 34,287.70

CASING PROTECTORS (WITHOUT LIPS) 261,741.70 — 10,615.00

13,181.33 TOTAL

PIPE WIPERS 12,296.00

1940
329,621.51

W LINE GUIDES 32,694.98 — ROYALTY 438.82

SWIVEL BUMPERS 7,797.61 — 658.77
MUD GUNS 2863.45 — 228.26
MUD GUNS (in royalty 5% 1/2) 1900.62 — 38.95

CASING PROTECTORS (WITHOUT LIPS) 70,758.23

8782.30

10,367.30 TOTAL

LIP PROTECTORS 163,000 (EST 70%)

SUCKER ROD PRO 1578.30
TUBING PROTECTORS 6527.20
PIPE WIPERS 30,089.30

SALE OF J.C. BALLAGH INVENTIONS 203,295.20 = 62%

1941
366,420.87

LINE GUIDES 34,938.84 — ROYALTY 412.58

MUD GUNS 3287.95 — 665.32
INSTALL EQUIPMENT 2252.40 — 38.43
CASING PROTECTORS (WITHOUT LIPS) 17,018.22

889.83

10,007.98 TOTAL

CASING PROTECTORS (WITH LIPS) 238,000 (EST 31%)

TUBING PROTECTORS 16,691.40

O PIPE WIPERS 43,862.20

SALE OF J.C. BALLAGH INVENTIONS 289,949.50 = 78.6%

EXHIBIT

TOTAL ROYALTY PAID

ITEM	PAID TO	1938	1939	1940	194
WIRE LINE GUIDE	REID	108.06	730.12	438.82	412.58
SWIVEL BUMPER	OYE & MEDEARIS	834.82	1,770.22	658.77	665.32
MUD GUN	TUEL		45.99	228.26	
SUCKER ROD WIPER	O'DELL			38.95	38.43
PROTECTORS	O-J & CONTINGENT	10,870.25	10,615.00	8782.30	8,688.83
TOTALS		12,813.13	13,181.33	10,367.30	10,007.98

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bodied in any resolution of the Board of Directors, no contract was produced; it was never mentioned to the Board of Directors.

Counsel refer to page 59 of the record, to our "puerile wail" that nothing was stated in the pleadings as to inventions, and that these inventions were first brought to light at the time of trial. There is more force to our statements than counsel realize. If the defendant Ballagh had been paid a salary not greater than warranted by his duties as Secretary-Treasurer and Sales Manager, and the balance of the compensation had been in the purchase and sale of inventions and patents, our action would have been for rescission of these transfers and for a refunding to the corporation of the moneys paid.

The Miller inventions. No weight can be given to these claimed inventions. At pages 46 and 47 of our opening brief we pointed out that they were infinitesimal. For the year 1940, out of gross sales of over $329,000, the sales that could be attributed to his inventions were only approximately $2,600, and in 1941, out of gross sales in excess of $366,000 the figure that could possibly be attributed to Miller was only approximately $6,000. The relative unimportance of his claim is best illustrated by reference to the defendants' Exhibit "A". The Miller inventions are shown at the very bottom of the 1940 and 1941 columns. In the original of Exhibit "A" they are shown in yellow.

The value of the Ballagh and Miller inventions. This subject is covered on pages 42-47 of our open-

ing brief, and counsel have given no convincing answer. We again bring up the same in light of defendants' Exhibit "A". That exhibit is misleading as to lip protectors. We quote from page 44 of our opening brief:

> "The casing protector business had existed ever since the formation of the Corporation; in fact had been taken over from the original partnership of Patterson & Ballagh. The defendants claim, however, that by invention they had improved the old casing protector by placing at each end thereof a so-called 'lip'. This was but a trivial improvement (R., 367). Not only does the testimony of the witnesses Chestnut and Grant so state (R., 544-545), but an examination of Exhibit E will so demonstrate.
>
> There is no showing that the Corporation's business would not have proceeded equally well without the claimed invention and, for that matter, no (*material number of*) lip protectors were sold in the year 1939 (R. 366), yet the protector business for that year substantially exceeded the protector business for the year 1940 and also for the year 1941. The witness Burrell admitted that the lip protector did not increase the protector business (R., 454)."

III. QUANTUM MERUIT.

At times counsel seems inclined to invoke *Quantum Meruit*. There are several answers.

(a) Numerous authorities are that when an officer performs services outside of his duties,

he must have a contract with the corporation before he can recover for such services. We cited these authorities upon page 40 of our opening brief.

(b) Section 3 of Article III of the By-laws precludes any such possibility. That By-law states "until the salary of an officer has been fixed by resolution of the Board of Directors, such officer shall serve without compensation" (R. 108). *Quantum Meruit* is based upon an implied contract. The By-law negatives any possibility of such implication.

(c) The defendants were dealing with themselves and prescribing by express resolution (contract) the amount of their salaries as president and general manager and secretary, treasurer and sales manager. They never suggested to the Board of Directors that they were entitled to payment on the basis of the value of their services. The value of their services was never considered. Furthermore, they put up no claim in this action either by cross-complaint or counter-claim or otherwise that there should be a determination of the value of their services as self-styled inventors. They themselves determined what they should receive in the capacities as shown by the minutes, and that was the end of it. They had no authority to, themselves, pass upon the value of their own services. Such right would be one only to be exercised by an independent board or this Court.

(d) The defendants were not rendering services by way of inventions. At best, certain property rights were transferred to the corporation. Furthermore these property rights were not worth anywhere near the consideration claimed by the defendants, whether in the form of salaries, or otherwise. These matters have been heretofore adequately considered.

IV. THE POWER OF THIS COURT TO REVERSE.

Counsel from pages 8 to 20 of their brief proper and from pages 1 to 10 of their appendix delve into a mass of cases having to do with whether the present action is one at law or in equity. They conclude that this is an action at law. Their conclusion is erroneous. (*Moon Motor Car Co. v. Moon,* 58 Fed. Rep. (2d) 90; *Wright v. Heublein,* 238 Fed. 321; *Green v. Felton,* 42 Ind. App. 675, 84 N. E. 166; *Raynolds v. Diamond Paper Mills Co.,* 69 N. J. Eq. 299, 60 Atl. 941; *Davis v. Thomas A. Davis Co.,* 63 N. J. Eq. 572, 52 Atl. 717; *Sotter v. Coatesville Boiler Works,* 257 Pa. 411, 101 Atl. 744.)[6]

We do not pursue the discussion. The question is moot. The third sentence of Rule 52 of the Rules of

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[6]Counsel mention that plaintiff has sought a joint judgment against both defendants. Although this is not material to the burden of proof, it is perfectly proper under the authorities. All directors who participate in the payment of illegal salaries are liable, even though they may not receive salaries themselves. In this case both Burrel and Armington, although not sued, were equally liable. *Atwater v. Elkhorn Valley Coal Land Co.,* 171 N. Y. S. 552; *Eshleman v. Keenan,* 21 Del. Ch. 259, 187 Atl. 25.

Civil Procedure for the District Courts of the United States is the answer. It states that if findings of fact are clearly erroneous they should be set aside. The rule adopted the modern Federal equity practice and is applicable to all classes of findings in cases tried without a jury, whether or not the finding is of a fact concerning which there was conflict of testimony or of a fact deducted or inferred from uncontradicted testimony. We stress, however, that there is no conflict in the facts upon which we rely, namely, the amount of defendants' salaries, the percentage of net profits which was thereby consumed, the ratio the salaries bore to the entire capital and surplus of the company, the years during which the so-called inventions were perfected, the lack of any authorization or contract for the employment of defendants as inventors, and so on.

We can do no better than quote from the Notes of the Advisory Committee appointed by the Supreme Court (Manual of Federal Procedure, p. 324), as follows:

> "See Equity Rule 70½, as amended Nov. 25, 1935 (Findings of Fact and Conclusions of Law), and U.S.C.A., Title 28, Sec. 764 (Opinion, findings, and conclusions in action against United States) which are substantially continued in this rule. The provisions of U.S.C.A., Title 28, Secs. 773 (Trial of issues of fact; by court) and 875 (Review in cases tried without jury) are superseded in so far as they provide a different method of finding facts and a different method of appellate review. The rule stated in the third sentence

> of Subdivision (a) accords with the decisions on the scope of the review in modern federal equity practice. It is applicable to all classes of findings in cases tried without a jury whether the finding is of a fact concerning which there was conflict of testimony, or of a fact deduced or inferred from uncontradicted testimony. See Silver King Coalition Mines Co. v. Silver King Consolidated Mining Co., 204 Fed. 166 (C.C.A. 8th, 1913), cert. den. 229 U. S. 624, 33 S. Ct. 1051, 57 L. Ed. 1356 (1913); Warren v. Keep, 155 U. S. 265, 15 S. Ct. 83, 39 L. Ed. 144 (1894); Furrer v. Ferris, 145 U. S. 132, 12 S. Ct. 821, 36 L. Ed. 649 (1892); Tilghman v. Proctor, 125 U. S. 136, 149, 8 S. Ct. 894, 31 L. Ed. 664 (1888); Kimberly v. Arms, 129 U. S. 512, 524, 9 S. Ct. 355, 32 L. Ed. 764 (1889). Compare Kaeser & Blair Inc. v. Merchants' Ass'n, 64 F. 2d 575, 576 (C.C.A. 6th, 1933); Dunn v. Trefry, 260 Fed. 147, 148 (C.C.A. 1st, 1919)."

Viewing counsel's argument from a more matter of fact angle, we add that this Court is not being asked to determine the extent of the excess of salaries. This may well be a matter for the trial Court. We are only asking this Court to state that the salaries were excessive and that the trial Court erroneously found to the contrary. This Court is in as good position to make such ruling as was the District Court. The evidence as to all matters material to this appeal was uncontradicted. *State Farm Mutual Automobile Insurance Co. v. Bonacci,* 111 Fed. 2, 412, relied upon at page 3 of the appendix to defendants' brief, recognizes the principle that where the lower court is in

no better position to judge than the appellate court, the appellate court is not bound by the findings.

The defendants during the years 1940 and 1941 extracted from the corporation salaries amounting to, respectively, 70% and 74% of the net profits. For those years they extracted salaries in an amount equivalent to one-quarter of the capital and surplus of the corporation. No increase in duties occurred.

Counsel at page 55 and elsewhere in their brief claim that the duties had been increased, due to the Bettis patent having been declared invalid; however, on page 47 of their brief they admit that the Bettis patent was declared invalid in the year 1932. The defendants are talking about the years 1932 to, at best, 1939. It is a fanciful flight of the imagination that increases in salaries made in 1939, 1940 and 1941 were on account of increases in responsibility occurring in the year 1932.

So far as counsel's argument is concerned, sometime during the year 1939 the curtain was rung down. We are talking about the years 1940 and 1941, when the peak of excessive salaries occurred. There is not one iota of testimony to justify salaries during those years, at any figures higher than would have been justified for an ordinary manufacturing business. Again we state that there is no necessity for us to rely upon the Bunch exhibit. That exhibit is only common sense, and accords with current facts. The experience and general knowledge of this Court is more than sufficient argument. Although it may surprise counsel,

cases of this type have been reversed. (*Ross v. Quinneses Mining Co.,* 227 Fed. 337; *Schall v. Althaus,* 203 N. Y. S. 36.)

V. THE BURDEN OF PROOF.

Counsel devote pages 20 to 43 of their brief and pages 10 to 20 of the appendix to an elaborate discussion attempting to establish the burden of proof to be upon the plaintiff. They resort to our claim of fraud. There may be some divergence in the authorities. We believe, however, that since the question is not one of substantive rights but one of evidence, the opinion of the United States Supreme Court should govern. We again quote from *Geddes v. Anaconda Mining Co.,* 254 U. S. 590, cited at pages 23 and 24 of our opening brief:

> "The relation of directors to corporations is of such a fiduciary nature that transactions between boards having common members are regarded as jealously by the law as are personal dealings between a director and his corporation, and where the fairness of such transactions is challenged the burden is upon those who would maintain them to show their entire fairness and where a sale is involved the full adequacy of the consideration. Especially is this true where a common director is dominating in influence or in character. This court has been consistently emphatic in the application of this rule, which, it has declared, is founded in soundest morality, and we now add in the soundest business policy. Twin-Lick Oil Co. v. Marbury, 91 U. S. 587, 588; Thomas v. Brownville Ft. Kearney & Pacific R. R. Co., 109

U. S. 522; Wardell v. Railroad Co., 103 U. S. 651, 658; Corsicana National Bank v. Johnson, 251 U. S. 68, 90."[7]

The point is not material. We have met the burden of proof. The real basis of recovery is the excessiveness of the salaries. Counsel has cited no opposing cases. Our view is well expressed in *Stratis v. Anderson,* 254 Mass. 536, 150 N. E. 832, and in the cases cited in that opinion, cited and quoted from at page 23 of our opening brief. For the convenience of the Court, we again quote:

> "It is immaterial in this connection whether there was actual fraud. The right of recovery for the benefit of the corporation rests upon the excessive payment to a director."

Not only the best way, but the only way to establish the excessiveness of salaries is to prove the amount thereof. Allegations and proof of other fraud may be determinative in a doubtful case but they are not essential if the mere amount of the salaries establishes their excessiveness.

Approaching this case from this angle, the mere proof of the amount of defendants' salaries was in itself sufficient to establish fraud or (if at all material to this case) to shift the burden of proof. Coun-

[7]Counsel mention sections 311 and 1963 of our California Code of Civil Procedure. Section 311 has nothing to do with the burden of proof. Section 1963 makes no mention of directors dealing with themselves. This section prescribes certain rules of evidence to be followed in state courts and, for the reason above given, would not be controlling even if this case were in a state court.

sel's own authority, *Nahikian v. Mattingly,* 265 Michigan 128, 251 N. W. 421, recognizes the foregoing, for, by the very excerpt quoted on page 11 of the appendix to defendants' brief, that case concedes that salaries can be, in themselves, so unreasonable or excessive as to be pronounced fraudulent without further proof.

Upon pages 36 and 41 of defendants' brief counsel also concede the foregoing. We quote as follows:

> "Where it clearly appeared as a matter of mathematical certainty that the consideration for the purchase assessed at its money value was inadequate, the plaintiff necessarily had sustained the burden of proof and the burden was thereupon cast upon the decedent to justify it. * * *" (Page 36)

> "* * * The claim was, in effect, that the discount he received for doing this and the profits he personally made in selling certain property of the corporation were excessive and unconscionable. A mere reading of the facts would seem to demonstrate that this was true. While the trial court found that the burden was on the company's receiver to prove fraud, the Appellate Court very properly holds otherwise.

> "The situation on the face of things showed the realization of large profits by Sisk on each of the transactions complained of which alone gives rise to a presumption that the property which he obtained from the corporation and resold was worth appreciably more than the price at which he obtained it from the corporation. * * *" (Page 41.) (Underscoring ours.)

If it is possible, let us assume a more extreme case than the one at bar. Suppose that the defendants by way of salaries for the year 1940 had extracted from the corporation the entire assets of the corporation over and above its indebtedness. The mere proof of that fact would be sufficient. In this case defendants extracted from 70% to 74% of the net profits and in each year an amount equivalent to one-quarter of the capital and surplus, all to the tune of $50,000 per year. The hypothetical case and the present case fall into the same category.

However, we are not saying that there was no other fraud. We believe that, in addition to at least the *prima facie* case made out by the very amount of the salaries, there was other fraud. This we showed in our opening brief and will hereinafter deal with the same again. This is our gratis contribution.

Counsel attempt at page 41 of their brief the argument that since Ballagh did not vote for his own increase in salary and Miller did not vote for his own increase in salary, the discretion of the Board of Directors can be upheld. Miller, however, did vote for Ballagh's increase, and Ballagh did vote for Miller's increase. The increases went hand in hand. The vote of each was given to increase the salary of the other. The language in *Angelus Securities Corp. v. Ball,* 20 Cal. App. (2d) 423, at 433, is pertinent. We quote therefrom as follows:

> "In the instant case, Woodward, Harriss, Ball and Crowe did not vote for their own salary, but

separate resolutions were introduced authorizing the salary, and while not voting for the resolution authorizing his own salary, each of the last-named directors voted for the resolutions authorizing a salary for the others. Six directors were necessary to constitute a quorum, and unless, for instance, Crowe, Harriss and Woodward were qualified to vote for Ball's salary, there was not a proper vote for that salary. Where, as in the instant case, the evidence shows that directors Ball, Crowe, Harriss and Woodward were interested in the common object of procuring a salary for each of them, the situation is not saved by passing several separate resolutions by a majority not interested in the particular resolution adopted. (Wonderful Group Min. Co. v. Rand, 111 Wash. 557 [191 Pac. 631, 633]; 14A Cor. Jur. 143, 144, sec. 1908.) The weight of authority seems to be that courts will not separate a resolution into parts and hold it valid on the ground that each part was carried by a majority of the votes of the other directors not interested in that particular portion, and this applies with equal force where several resolutions are introduced upon the same theory. The fact that a resolution increasing salaries is voted on in parts, so that no director votes on the proposition to increase his own salary, does not justify the passage of the salary resolution, because the effect is merely to give a semblance of legality to a wrongful act. (Davids v. Davids, 135 App. Div. 206 [120 N. Y. Supp. 350].) As to the third cause of action the nonsuit should have been denied."

See also *Sagalyn v. Meekins, Packard and Wheat,* 290 Mass. 434, 195 N. E. 769, 771.

Counsel, by sidestepping the foregoing authorities, forget that in this case the defendants, as directors, were dealing with themselves. There is no conflict on this point. Dulin consistently voted against and vigorously protested the salary increases. The other directors, Burrell and Armington, were dominated by the defendants, and, even had they not been so dominated, the vote of Miller was given for the Ballagh raises and the vote of Ballagh for the Miller raises. In the language of counsel, when such a showing is made (if the burden of proof was ever upon the plaintiff) the burden shifted to the defendants.

At page 40 of defendants' brief in commenting upon *Church v. Harnit,* 35 Fed. (2d) 499, the following appears:

> "* * * In other words, the directors who voted the bonus to Harnit in the first place were, in fact, voting a bonus to themselves since it was understood in advance that Harnit would pay portions of the bonus voted to him to them and, under these circumstances, the Court holds that the burden was upon the directors voting for the bonuses which they eventually received to show that they were fair and reasonable."

After the foregoing, there appears upon page 41 of counsel's brief the following:

> "* * * This is simply another of many cases which hold that where a director does himself par-

ticipate in the vote affording him increased compensation without a corresponding increase in his duties and responsibilities, the burden is cast upon him to establish his fair dealing, which is not at all the case at bar."

On page 42 counsel further state:

"* * * Here again is a case, of which there are many, which lays down the rule that where the beneficiary of the vote participates in the voting, the courts will scrutinize the action of the board and the burden is shifted to the participating director to establish the fairness of the board's action."

Also worthy of further comment is that in the excerpt from defendants' brief above quoted from page 41 thereof they admit that a director who votes for a resolution increasing his own compensation without corresponding increase in his duties and responsibilities takes over the burden of proof. Here, there was no increase in duties or responsibilities.

At page 22 of our opening brief we showed the control that the defendants exercised over the corporation.[8] At pages 5 and 48 of our opening brief

[8]In an attempt to argue against what has been firmly established by the record that the defendants exercised complete control over the corporation, counsel mentioned certain circumstances, to-wit:

(a) They claim that the defendants managed the corporation "subject to the direction of the Board". This may be correct, but the defendants were the Board. Burrell and Armington only acted for these defendants. No majority could be obtained unless Miller or Ballagh voted.

(b) They claim that the defendants were very solicitous of the prerogatives of Dulin as a director. The defendants certainly were

we pointed out that just as soon as Miller bought into the corporation he not only proceeded to increase salaries, but also repudiated all obligation to pay plaintiff royalties under Exhibits 15A, 15B, 15C and 15D (R. 222; 229; 336; 359; 382),[9] and also refused the payment of any further dividends (R. 68; 245; 255; 382). In other words, in accordance with the authorities cited on page 49 of our opening brief, the defendants were resorting to the unlawful practice of distributing corporate profits in the guise of compensation.

If anything further is required to establish fraud, we again refer to our argument at page 51 of our

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not solicitous when it came to fixing their own salaries and that they may have been in other respects is immaterial.

(c) They argue that on one occasion both Patterson and Rennie voted with Dulin. Patterson ceased to be a director when defendant Miller bought into the Company and Rennie over the protest of Dulin was thrown off the Board at the meeting of February 2, 1939. He was not the type of director that the defendants wanted.

(d) They argue that Dulin voted for certain increases of salary (not those attacked in this case). These increases occurred in October of 1938, and March of 1939. Neither of these raises could be material; furthermore, their peak was $1,500 per month, which is a far cry from the amount of defendants' salaries during 1940 and 1941.

It may well be that Dulin was too liberal in voting for the increases for which he did vote and as above mentioned. It may well be that his action was in an attempt to keep peace in the family trusting that the defendants might thereby be persuaded to treat the minority stockholders to some extent in a fair manner. The truth is that the subsequent increase of salaries over the objections of Dulin got out of all bounds—thus this present action.

[9]As mentioned on page 48 of our opening brief, Mr. Judge Hollzer held that the repudiation of royalties by the defendants was wrongful. That case is now on appeal entitled "Patterson Ballagh Corporation, Appellant, vs. Byron Jackson Co., Appellee" and is numbered 10,553 upon the records of this court.

opening brief, namely that Ballagh testified that the defendants did not consider their cash on hand adequate to pay dividends (R. 361); nevertheless, they raised their own salaries and in so doing, admittedly by their testimony, took into consideration the fact that they were not paying dividends (R. 358; 363; 382). If more is needed, we again refer to the Miller letter of August 22, 1939 which was sent about the time that the conspiracy between Ballagh and Miller was hatched. We again quote from that letter:

> "Since assuming office as President of Patterson-Ballagh Corporation I have taken upon myself the duty of studying the various costs in connection with the conduct of this business. I find that for the first six months of 1939, the corporation will show a loss of some $2,000. (R., 223.)"

We cannot conceive that any stronger evidence of fraud could be produced in a case of this character, except possibly by the express admissions of fraud by the defendants themselves.

Fraud need not consist of being caught "red-handed", with a marked bill or a "rubber check". The fraud in this case was of the type that simmered and planned and conspired and then burst into flame.

VI. RATIFICATION AND WAIVER.

Counsel devote two pages, to-wit 76 and 77, of their brief to the contention of ratification and waiver. They overlook three very pertinent elements:

1. The conclusions of law of the trial judge held that a waiver existed only for the period from January 1, 1941 to September 10, 1941.

2. Counsel neglect the long line of authorities (as to which we know none in opposition) that majority stockholders are bound to exercise the same good faith as majority directors, and may not, for selfish purposes, act in hostility to the interests of the corporation with the intent of defrauding the non-assenting stockholders. We quote from *Godley v. Crandall & Godley Co.*, 212 N.Y. 121, 105 N.E. 818:

> "A majority of the stockholders, consisting of those who had received the preferential payments, voted after the commencement of this action to ratify the acts of the directors. But even majority stockholders may not for selfish purposes act in hostility to the interests of the corporation with the intention of defrauding the non-assenting stockholders. Gamble v. Queens County Water Co., supra; Farmers' Loan & Trust Co. v. N. Y. & N. Ry. Co., 150 N. Y. 410, 44 N. E. 1043, 34 L. R. A. 76, 55 Am. St. Rep. 689; Flynn v. Brooklyn City R. R. Co., supra; Continental Securities Co. v. Belmont, 206 N. Y. 7, 99 N. E. 138, Ann. Cas. 1914A, 777. The recovery under this head, as modified by the Appellate Division was proper."

We also cite: *Atwater v. Elkhorn Valley Coal Land Co.,* 171 N. Y. S. 552; *Collins v. Hite,* 109 W. Va. 79, 153 S. E. 240; *Barrett v. Smith,* 185 Minn. 596, 242 N. W. 392; *Sotter v. Coatesville Boiler Works,* 257 Pa. 411, 101 Atl. 744, p. 747.

3. Also, the following appears in the minutes of the annual meeting of shareholders held January 21, 1941, the meeting at which the waiver and ratification was supposed to have occurred, to-wit:

> "Thereupon, on motion of J. C. Ballagh, seconded by D. G. Miller and carried, E. S. Dulin voting in the negative, it was
>
> Resolved, that all action taken by the Board of Directors of this corporation since the date of the last annual meeting of the shareholders, whether said Directors were de facto or de jure, and all action of the officers of this corporation done pursuant to the authorization of the Board of Directors or with the knowledge and acquiescence of the Directors are hereby ratified, approved and confirmed as and for the corporate acts of this corporation.
>
> E. S. Dulin explained his vote in the negative on the foregoing resolution by stating that in his opinion the acts of the officers and Directors in accepting and fixing the amount of compensation paid during the last fiscal year to the President and Secretary was contrary to the best interests of the minority shareholders."

We respectfully submit that the judgment should be reversed and the cause remanded for a new trial.

Dated, San Francisco, California,
November 26, 1943.

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The case of Caminetti v. Prudence Mutual Life Ins. Assn., 61 A. C. A. 67, quoted in full in the following appendix has just come to the attention of the writer of this brief. It is too late to argue from the same. The case, however, involves so many similar points that we set it forth at length without comment.

Appendix.

Appendix

(Vol. 61 A. C. A. 67.)

In the District Court of Appeal
State of California
Second Appellate District

Division Three

2 Civil No. 13,918

A. Caminetti, Jr., as Insurance Commissioner, etc.,
Appellant,
vs.
Prudence Mutual Life Insurance Association (a corporation),
Respondent.

[1a, 1b] Insurance—Corporations—Insolvency—Conservator — Termination — Appeal—Harmless and Reversible Error.—On hearing of an application to terminate the Insurance Commissioner's conservatorship over the property and business of an incorporated insurance association, an erroneous ruling that the commissioner was required to proceed first with the production of evidence was not a ground for reversal where all of the evidence of both parties was fully presented.

[2] **Appeal — Presumptions — Evidence—Burden of Proof.**—Where the trial court vacated an erroneous ruling on the burden of proof, it will be presumed on appeal that the court thereafter considered the evidence in the light of the proper rule as to burden of proof.

[3] **Insurance—Corporations—Insolvency—Conservator—Termination—Rules of Procedure.**—An application under Ins. Code, § 1012, to terminate the Insurance Commissioner's conservatorship over the property and business of an incorporated insurance association is a special statutory proceeding, and the rules of procedure for ordinary civil actions do not apply to such proceeding of their own force.

[4] **Id. — Corporations — Insolvency—Conservator—Application.**—No provision having been made for an appearance in response to a verified application for conservatorship filed by the Insurance Commissioner under Ins. Code, § 1011, that application is evidently not a complaint to be answered.

[5] **Id.—Corporations — Insolvency — Conservator—Termination—Application.**—If an incorporated insurance association desires vacation of an order appointing the Insurance Commissioner as con-

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McK. Dig. References: [1, 3-8, 15-17] Insurance, § 11; [2] Appeal and Error, § 1136; [9, 12] Corporations, § 595; [10, 11] Corporations, § 595; Husband and Wife, § 61; [13] Compromise and Settlement, § 1; [14] Insurance, § 234.

servator of its property and business, the association must present its own application therefor.

[6] **Id.—Corporations — Insolvency—Conservator—Termination—Nature of Proceeding.**—A proceeding to terminate the Insurance Commissioner's conservatorship over the property and business of an incorporated association is not like that of an order to show cause and restraining order issued to one seeking an injunction. The commissioner need do nothing after the order appointing him as conservator, and if the association does nothing the order continues in force indefinitely.

[7] **Id.—Corporations — Insolvency—Conservator—Termination—Evidence—Burden of Proof.**—In a proceeding under Ins. Code, § 1012, the burden of proof is on the corporation challenging continuance of the Insurance Commissioner's conservatorship over its property and business, to make it "appear to the court" that there are proper reasons for setting aside the conservatorship.

[8] **Id.—Corporations — Insolvency—Conservator—Persons Affected.**—The word "person," as used in Ins. Code, § 1011, enumerating the conditions affording ground for an order appointing the Insurance Commissioner as conservator of an insurance company, includes corporations and associations.

[9] **Corporations—Officers—Vote of Interested Director.**—The former rule that a corporation director was disqualified from voting on any matter in

which he was directly and personally interested, was modified by the adoption of Civ. Code, § 311, which declares that no transaction between a corporation and one of its directors shall be void because such director is present at the meeting at which the transaction is authorized, if, among other things, the fact of his interest is known to the board and the transaction is authorized by a vote sufficient without counting that of such director.

[10] **Id.—Officers—Vote of Interested Director: Husband and Wife—Property—Community and Separate—Husband's Salary.**—The resolutions of a corporation board of directors consisting of three persons, of whom a husband and wife were two, fixing the salary of the husband, and a subsequent resolution authorizing the compromise of his claim for back salary, were not passed by a majority sufficient for that purpose without his vote, and the transaction could not be upheld under Civ. Code, § 311(a). The wife's vote could not be counted to carry the resolution fixing her husband's salary, as such salary would be community property under Civ. Code, § 164, and by virtue of Civ. Code, § 161a, she would have a present and equal interest therein.

[11] **Id.—Officers—Vote of Interested Director: Husband and Wife—Property—Community and Separate—Wife's Earnings.**—Where two of the three

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[9]See 6A **Cal.Jur.** 1107; 13 **Am.Jur.** 955.

directors of a corporation were husband and wife, and where the resolution compromising the wife's salary claim and that of the husband came up for action in the same meeting, they were interested in the common object of obtaining more salary for each of them and were both disqualified to vote on either resolution. The husband, however, was not disqualified to vote on the original resolutions fixing the wife's salary where they were living apart at the time, as her earnings during such period would be her separate property under Civ. Code, § 169.

[12] **Id.—Officers—Compensation—Implied Contract.**—An officer who renders beneficial services to a corporation, without any lawful action of the board of directors fixing his compensation, but under circumstances negativing an intent that they were to be gratuitous, may recover the reasonable value of those services. But no recovery may properly be allowed for such services where there is no evidence that the services rendered to the corporation by the officer, during the time to which his claim for back salary relates, were worth more than he had received for them.

[13] **Compromise and Settlement—Good Faith of Parties.**—The rule that a compromise of a claim asserted in good faith is valid even though the claim is actually without legal foundation, has no application where the claimants, acting as fiduciaries for the adverse party, approve the com-

promise of their own claims and the approval fails for that reason.

[14] **Insurance—Contribution.**—The fact that a husband and wife, who were paid the amount of a compromise of their claims for back salaries as officers of an incorporated insurance association, had agreed to make a "contribution" of the amounts received to the association under Ins. Code, § 10745, did not prevent any part of the payments on the compromise from being a diversion of the association's assets, where the "contribution," was not a gift, but an advancement, to be repaid to the contributor when the condition of the association should warrant.

[15] **Id.—Corporations—Insolvency—Conservator—Wrongful Diversion of Corporation's Assets.**—Payments to officers of an incorporated insurance association upon an unauthorized compromise of their claims for back salaries, constitute a wrongful diversion of the association's assets, within the meaning of Ins. Code, § 1011, subd. (h). It is not necessary that the wrongful diversion should be akin to embezzlement, as the word "embezzlement" appears in the statute in addition to the words "wrongfully diverted," and under the rule of statutory construction, that meaning and effect are to be given to every word and clause of a statute, the ordinary meaning of the words "wrongfully diverted" is sufficient for that purpose.

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[15] See 23 **Cal.Jur.** 758.

[16] **Id.—Corporations—Conservator — Termination —Evidence—Burden of Proof.**—An incorporated insurance association seeking to terminate the Insurance Commissioner's conservatorship over its property and business has the burden of proving that it can properly resume title and possession of its property and the conduct of its business, as required by Ins. Code, § 1012. Whether there is evidence to justify a finding for the association on this issue is a matter primarily for the consideration and the discretion of the trial court, whose decision is binding on appeal unless without any support in the evidence.

[17] **Id.—Corporations—Conservator — Termination —Construction of Statute Authorizing.**—In Ins. Code, § 1102, requiring, as a prerequisite to an order terminating the Insurance Commissioner's conservatorship of an insurance corporation, that the ground on which he was made conservator "does not exist or has been removed," the words "does not exist," although couched in the present tense, refer to the time when the order appointing the conservator was made; otherwise there would be no use in the statute for the other alternative, "or has been removed."

APPEAL from a judgment of the Superior Court of Los Angeles County. Thurmond Clarke, Judge. Reversed.

Application by insurance association to terminate conservatorship of Insurance Commissioner over its property and business. Judgment dissolving conserv-

atorship and directing restoration of property and business to insurance association, reversed.

Robert W. Kenny, Attorney General, and John L. Nourse, Deputy Attorney General, for Appellant.

Chas. R. Thompson, Sherman & Sherman and Ralph H. Lewis for Respondent.

SHAW, J. pro tem.—Appellant, as Insurance Commissioner of the State of California, obtained from the Superior Court of Sacramento County an order under section 1011 of the Insurance Code appointing him as conservator of the business of the respondent, Prudence Mutual Life Insurance Association, and pursuant to this order took over its property and business. The respondent is a corporation organized to do life insurance business on the mutual benefit assessment plan. Corporations of this class are usually referred to in the Insurance Code as "associations." As soon as this order was made, the proceeding was transferred to Los Angeles County. Later, on application of respondent, a hearing was had under section 1012 of the Insurance Code, at the conclusion of which the Superior Court of Los Angeles County entered a judgment cancelling and terminating the former order, dissolving the conservatorship and directing the restoration to respondent of its property and business. From this judgment the Insurance Commissioner appeals.

[1a] At the outset of the hearing the trial court was asked to rule upon the question where lay the burden of proof, and after extended argument it announced its opinion that the burden rested on the In-

surance Commissioner. Appellant now complains of this as reversible error. The court's declaration of law, although erroneous, as will presently appear, does not in itself afford ground for a reversal, under the circumstances of this case. As a result of this declaration the commissioner's evidence was produced first, but it does not appear that either party was prevented by it from producing all available evidence, or desired to or could obtain or present anything further. The hearing appears to have been a "full hearing," as required by section 1012 of the Insurance Code. [2] After the taking of evidence, and just before the entry of judgment, the trial court made an order vacating the submission of the case and reopening it for the purpose of making and did make a further order vacating its ruling on the burden of proof and declaring that it had heard, considered and weighed all of the evidence of both parties and that "regardless of where the burden of proof lay, the decision of this court would not be affected." This order was made seven days after the filing of the first of the decisions on burden of proof hereinafter cited and we are informed by the briefs that it was made by reason of that decision. However that may be, it shows that the court vacated its ruling on the burden of proof. We must therefore presume, nothing now appearing to the contrary, that the court weighed and considered the evidence in the light of the proper rule as to the burden of proof. [1b] The only remaining effect of its former ruling is that the appellant was required to proceed first with the production of evidence. But an error in that respect does not ordi-

narily result in a miscarriage of justice, where all the evidence of both parties is fully presented, and we think it did not here.

In spite of this conclusion it is necessary for us to deal with the question of the burden of proof, for appellant contends that there is no proof of various facts essential to the support of the judgment, that respondent had the burden of proving those facts, and that the lack of proof of them requires a reversal. The Insurance Code contains, in article 14 of chapter 1, part 2, division 1, comprising sections 1010 to 1062, elaborate provisions for proceedings in case of insolvency or delinquency of "persons" (defined by section 19 to include associations and corporations) doing insurance business. Section 1011 provides that the Superior Court "shall, upon the filing by the commissioner of the verified application showing any of the following conditions hereinafter enumerated to exist" make an order vesting in the commissioner title to all the assets of an insurance company and directing him to take possession of its records and assets, and to conduct, as conservator, its business. This application must be served on the company ("person") in the same manner as a summons (sec. 1040), but no provision is made for an answer to it, and the order mentioned in section 1011 is obviously to be made ex parte on the filing and presentation of the application. Section 1012 provides as follows: "Said order shall continue in force and effect until, on the application either of the commissioner or of such person [company], it shall, after a full hearing, appear to said court that the ground for said order

directing the commissioner to take title and possession does not exist or has been removed and that said person can properly resume title and possession of its property and the conduct of its business."

[3] It is clear that what we have here is not an ordinary civil action, but a special statutory proceeding. None of the rules of procedure for such actions are made applicable to it by the statute (except as already noted) and they do not apply to it of their own force. (*Carpenter v. Pacific Mut. Life Ins. Co.*, (1937) 10 Cal.2d 307, 327-8 [74 P.2d 761]; *Carpenter v. Pacific Mut. L. Ins. Co.*, (1939) 13 Cal.2d 306, 311 [89 P.2d 637].) **[4]** No provision is made for an appearance in response to the verified application filed by the commissioner under section 1011, and that application is evidently not a complaint to be answered. **[5]** The company, if it desires a vacation of the order, must present its own application therefor. While the statute does not require it to state in such application any reasons for vacation of the order, no doubt it may do so. Such reasons may or may not include a negation of the grounds of the order, but if they do it comes as the claim or contention of the company so applying. The original application of the commissioner has served its purpose when an order has been made upon it, except as a place of reference to ascertain the grounds of the order.

[6] Nor is the proceeding at all like that in case of an order to show cause and restraining order issued to one seeking an injunction. Such a party is the actor and must proceed with his proof or lose his restrain-

ing order. Here the commissioner need do nothing after obtaining the order appointing him as conservator; and if the company does nothing the order continues in force indefinitely.

Even if the company obtains a hearing, the order, by the terms of section 1012 "shall continue in force and effect until . . . it shall, after a full hearing, appear to said court" that for the reasons stated in this section it should be set aside. If at the hearing there is no evidence at all, or the evidence presented is insufficient to prove, that is, make it "appear to the court," that there are proper reasons for setting aside the order made under section 1011, the company, if it is the applicant for such relief, must fail. **[7]** A statutory provision with this effect places the burden of proof on the party who must meet its requirements to succeed. This is in conformity to the provisions of section 1981, Code of Civil Procedure, that "the burden of proof lies on the party who would be defeated if no evidence were given on either side." The same conclusion has been reached, for somewhat different reasons, with which, also, we agree, in *Caminetti v. Guaranty Union L. Ins. Co.* (1942) 52 Cal.App.2d 330, 337 [126 P.2d 159], and *Caminetti v. Imperial Mut. L. Ins. Co.,* (1943)[1] 59 Cal.App.2d 476, 487 [139 P.2d 681].

Section 1011 of the Insurance Code enumerates among the conditions, the existence of which affords ground for an order appointing the Insurance Commissioner as conservator of an insurance company, the

[1]Advance Report Citation: 59 A.C.A. 584, 595.

following: "(d) That such person is found, after an examination, to be in such condition that its further transaction of business will be hazardous to its policy holders, or creditors, or to the public. . . . (h) That any officer or attorney-in-fact of such person has embezzled, sequestered, or wrongfully diverted any of the assets of such person." [8] The word "person" here, as elsewhere in the code, by definition includes corporations and associations. The commissioner's application for the order in this case stated as a ground therefor that two of the officers of respondent, Charles E. Fielder and his wife, Eunice H. Fielder, had wrongfully diverted assets of the association to themselves. This charge is based on the compromise and payment of claims for back salary made against the association by them. During the whole time covered by the inquiry Charles E. Fielder was a director and general manager of the association and also held either the office of president or that of secretary and his wife, Mrs. Eunice H. Fielder was office manager and vice president and also a director. In February of 1931, 1932, 1933 and 1934, the board of directors of the association consisted of three persons, of whom Mr. and Mrs. Fielder were two, and in each of these months the board adopted a resolution fixing the salary of the "secretary and general manager" at $400 per month and another resolution fixing the salary of the "vice president and assistant secretary" at $200 per month. Apparently all the directors voted for all of these resolutions. The next action taken by the board of directors on officers' salaries was a resolution

adopted on September 7, 1935, fixing the salaries of the officers at a maximum of $200 per month "during the existing emergency." In August, 1935, Mr. and Mrs. Fielder signed waivers of all unpaid salaries up to July 31, 1935. No further action regarding officers' salaries was taken up to the time of the compromises hereinafter mentioned. From July 31, 1936, to August 1, 1939, C. E. Fielder drew a salary of $200 per month and Mrs. Fielder drew a salary of $75 per month. On September 5, 1939, Mr. and Mrs. Fielder presented to the board of directors claims for back salaries, Mr. Fielder's for $5,000, and Mrs. Fielder's for $4,775, each of them also making an offer to compromise for $2,550. On September 13, 1939, the board of directors, at a meeting at which Mr. and Mrs. Fielder and one other director were present, adopted separate resolutions, for which all the directors voted, authorizing the acceptance of these offers of compromise and the compromise of each of these claims for $2,550. Following these resolutions the amounts of the compromises were paid to Mr. and Mrs. Fielder.

[9] The law in California formerly was that a director was disqualified from voting on any matter in which he was directly and personally interested and could not be one of a majority essential to the adoption of such a resolution. (6A Cal.Jur. 1107; *Angelus Securities Corp. v. Ball,* (1937) 20 Cal.App.2d 423, 432, [67 P.2d 152].) That rule was somewhat modified by the adoption of section 311 of the Civil Code, which as it now stands declares that no contract or other transaction between a corporation and one of

its directors, or between a corporation and any corporation, firm or association in which one of its directors is financially interested, shall be void or voidable by reason of the fact that such director is present at the meeting at which the contract or transaction is authorized or approved or that his vote is counted for that purpose, if (a) the fact of his interest is known to the board and the contract or transaction is authorized or approved by a vote sufficient without counting that of such director, or (b) the contract or transaction is approved or ratified, with knowledge of the director's interest, by a majority of the shareholders, or (c) the "contract or transaction be just and reasonable as to the corporation at the time it was authorized or approved."

[10] It is clear that, as far as Mr. Fielder is concerned, the original resolutions fixing his salary and the resolution authorizing the compromise were not passed by a majority sufficient for that purpose without his vote, and hence the transaction cannot be upheld under subdivision (a) of section 311, above referred to. His salary, as well as any amount received in compromise of a claim therefor, would be community property (Civ. Code, sec. 164), and by virtue of section 161a of the Civil Code, adopted in 1927, his wife would have a present, existing and equal interest therein. Possibly Mrs. Fielder's vote on her husband's salary is not within the letter of section 311 of the Civil Code, since he is neither a corporation, a firm nor an association; but if not, it is within the rule which governed prior to the adop-

tion of that code provision and there is nothing in section 311 to prevent the continuing application of the former rule to cases not within the purview of this section. In either case Mrs. Fielder's vote could not be counted to carry the resolution fixing her husband's salary. *Cuneo v. Giannini,* (1919) 40 Cal. App. 348 [180 P. 633], which appears to hold to the contrary, was decided before the adoption of section 161a of the Civil Code.

It is to be noted also that while the salary fixing resolutions under which Mr. Fielder made his claim fixed the salary of the "secretary and general manager," which positions he held when the resolutions were passed, he ceased to be secretary and became president on November 3, 1937, and so remained until August 3, 1939. This interregnum extended over nearly the whole period of time for which he claimed back salary, and during it the salary fixing resolutions above mentioned did not cover him. Apparently there was no resolution fixing a salary for the president alone or for the general manager alone, or for both officers together.

[11] Mrs. Fielder's vote for the compromise of her husband's claim also fails for another reason. The resolutions compromising her salary claim and that of Mr. Fielder came up for action at the same meeting. Before this meeting they talked the matter over and agreed to both compromises. They thus became interested, if they were not before, in the common object of obtaining more salary for each of them and were both disqualified to vote on either resolution.

(*Angelus Securities Corp. v. Ball, supra,* (1937) 20 Cal.App.2d 423, 433.)

For the reason last stated Mr. Fielder was also disqualified from voting on the resolution compromising Mrs. Fielder's claim. Apparently he was not interested in her salary as community property, and hence was not disqualified to vote on the original resolutions fixing her salary. Both parties state in their briefs that Mr. and Mrs. Fielder were living separate and apart and while they give us no record reference for that fact and we have found none, we are disposed to accept the fact thus agreed on. Her earnings while she is living separate from her husband being her separate property (Civil Code, sec. 169), he would not be disqualified from voting upon them.

The compromise was not submitted to the shareholders—indeed, this corporation had no shareholders —and hence is not affected by subdivision (b) of section 311 of the Civil Code. **[12]** Respondent contends that it may be upheld under subdivision (c) on the ground that it was just and reasonable as to the corporation. As to that, we begin with the fact that there was no valid resolution fixing the salary of Mr. Fielder. However, it is held that an officer who renders beneficial services to a corporation, without any lawful action of the board of directors fixing his compensation, but under circumstances negativing an intent that they were to be gratuitous, may recover the reasonable value of those services. (*Bassett v. Fairchild,* (1901) 132 Cal. 637 [64 P. 1082, 52 L.R.A.

611]; *Andrews v. Glick,* (1928)205 Cal. 699 [272 P. 587].) Respondent seeks to support the judgment here under this rule. However, we can find no evidence which would support a finding that the services rendered to the corporation by Mr. Fielder during the time to which his claim for back salary relates were worth more than he had received for them. Since the burden of proof was upon respondent in this proceeding, a defect of proof in this respect would require a finding against respondent. While the respondent states in its brief that the record "is replete with testimony of what duties they [the Fielders] performed," no reference is made to any such testimony and we have discovered none. There is testimony showing that respondent was in bad condition financially at the beginning of this period and in greatly improved condition at the end of it. But this is not enough. We find nothing showing how much time, effort and attention on the part of the officers were necessary or applied to produce such a result. The association was a small one and its administration may have been a part time job. It does appear that the salaries claimed by the two officers would, for most of the period covered by their claims, amount to 20 per cent or more of the income of the association. It further appears that no liability for these back salaries was set up on the books of the association or mentioned in any of its published statements of condition; and that Mr. and Mrs. Fielder received and accepted the salaries paid them without manifesting any objections to them.

[13] Respondent also attempts to support the compromises by reference to the rule that a compromise of a claim asserted in good faith is valid even though the claim is actually without legal foundation. That rule can have no application in a case like this where the claimants, acting as fiduciaries for the adverse party, approve the compromise of their own claims and the approval fails for that reason.

[14] Respondent further claims that the payment of these sums to Mr. and Mrs. Fielder did not constitute a diversion of the association's assets because they had agreed [with each other] to make a "contribution" of the amounts received (less $50 each) to the association under section 10745 of the Insurance Code. However, this arrangement for a "contribution" did not prevent any part of the payments on the compromise from being a diversion. The "contribution" was not a gift, but an advancement, to be repaid to the contributor when the condition of the association should warrant. Section 10745, under which the contributions would be made, while it provides that the "obligation to return such money shall not be a liability or claim . . . against the association" also provides that the "return of such money . . . shall be payable only out of surplus remaining after providing for all required reserves, surplus, or minimum funds and other liabilities, whether required by the laws of this State or any other State in which the association does business," and section 10748, relating to the same subject, provides that when such an association discontinues business, after all claims and

liabilities are paid or provided for "any surplus shall be returned to the person who advanced it."

[15] Respondent also argues that these payments to officers of the association upon the unauthorized compromise of their claims, which in the case of at least one of them appear to be without any legal foundation, do not constitute a wrongful diversion of the assets of the association within the meaning of Subdivision (h) of 1011 of the Insurance Code, the contention being that "the wrongful diversion would have to be akin to embezzlement and be of a deliberate fraudulent or felonious nature." One answer to this argument is, that the statute, in describing the acts which subject an insurer to seizure, uses the words "embezzled" and "sequestered" in addition to "wrongfully diverted." Since the word "embezzled" thus appears in the statute, we must, following the rule of statutory construction that meaning and effect are to be given to every word and clause of a statute, if that is reasonably possible (23 Cal.Jur. 758-9), seek some meaning other than that of embezzlement for the words "wrongfully diverted." The ordinary meaning of the words is sufficient for that purpose. The payment of funds of the association to the two officers constituted a diversion of those funds to them, and since there was no legal authority for the payment, the diversion was wrongful. Nothing further was needed to bring the case within the statutory provision in question. (See *Wickersham v. Crittenden,* (1892) 93 Cal. 17, 32 [28 P. 788]; same case, (1895) 106 Cal. 327 [39 P. 602];

also *People v. Talbot,* (1934) 220 Cal. 3, 15 [28 P.2d 1057].)

[16] Finally, section 1012 of the Insurance Code, requires that before an order such as that here appealed from can be made it shall appear that the insurer "can properly resume title and possession of its property and the conduct of its business." On this issue, also, the respondent had the burden of proof, and appellant insists that there is no evidence justifying a finding in respondent's favor thereon. This is a matter primarily for the consideration and discretion of the trial court, whose decision is binding on appeal unless without any support in the evidence. (*Caminetti v. Guaranty Union L. Ins. Co., supra,* (1942) 52 Cal.App.2d 330, 336 [126 P.2d 159]; *Caminetti v. Imperial Mut. L. Ins. Co., supra.* (1943) 59 Cal.App.2d 476, 486 [139 P.2d 681].) While there is evidence here which would have supported a finding against the respondent on this issue, we cannot say there is no reasonable view of the evidence which would support the trial court's implied finding in its favor. However, this conclusion does not require us to affirm the judgment. **[17]** Section 1012 of the Insurance Code further requires, as a prerequisite to such an order as we have here, a showing, in the alternative, that the ground on which the commissioner was made conservator "does not exist or has been removed." The first of these alternatives, "does not exist," although couched in the present tense, undoubtedly refers to the time when the order appointing the conservator was made. If it were not

so construed, there would be no use in this provision for the other alternative, "or has been removed," for a condition that has been removed necessarily does not exist. This would again run counter to the rule of construction above mentioned, that meaning and effect shall be given every word of a statute. As we have already shown, the ground of action existed here when the order was made; and there is no showing that it has been removed, for the diverted funds appear to be still diverted. We are not undertaking here to decide whether such an act of diversion, once done, can be undone so as to remove the ground of such an order. We merely suggest the question as one which may require future consideration.

The judgment appealed from is reversed.

Shinn, Acting P. J., and Wood (Parker), J., concurred.

Filed October 18, 1943,
James E. Brown, Clerk.